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Bankers and Chancellors

William W. Bratton
University of Pennsylvania Law School, wbratton@law.upenn.edu

Michael L. Wachter
University of Pennsylvania Law School, mwachter@law.upenn.edu

Articles

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William W. Bratton* & Michael L. Wachter**

The Delaware Chancery Court recently squared off against the investment banking world with two rulings that tie Revlon *violations to banker conflicts of interest. Critics charge the court with slamming down fiduciary principles of self-abnegation in a business context where they have no place or, contrariwise, letting culpable banks off the hook with ineffectual slaps on the wrist. This Article addresses this controversy, offering a sustained look at the banker–client advisory relationship. We pose a clear answer to the questions raised: although this is nominally fiduciary territory, both banker–client relationships and the Chancery Court's recent interventions are contractually driven. At the same time, conflicts of interest are wrought into banker–client relationships: the structure of the advisory sector makes them hard to avoid and clients, expecting them, make allowances. Advisor banks emerge in practice as arm's-length counterparties constrained less by rules of law than by a market for reputation. Meanwhile, the boards of directors that engage bankers clearly are fiduciaries in law and fact and company sales processes implicate enhanced scrutiny of their performance under* Revlon*.* Revlon *scrutiny, however, is less about traditional fiduciary self-abnegation than about diligence in getting the best deal for the shareholders. The Chancery Court's banker cases treat conflicts in a contractual rather than fiduciary frame, standing for the proposition that a client with a* Revlon *duty has no business consenting to a conflict and then passively trusting that the conflicted fiduciary will deal in the best of faith. The client should instead treat the banker like an arm's-length counterparty, assuming self-interested motivation on the banker's part and using contract to protect itself and its shareholders. As a doctrinal and economic matter, the banker cases are about taking contract seriously and getting performance incentives properly aligned and not about traditional fiduciary ethics. They deliver considerably more than a slap on the wrist, having already ushered in a demonstrably stricter regime of conflict management in sell-side boardrooms. They also usher in the Delaware Chancery Court itself as a focal-point player in the market for banker*

* Deputy Dean and Nicholas F. Gallicchio Professor of Law; Co-Director, Institute for Law & Economics, University of Pennsylvania Law School. Our thanks to Deborah DeMott, Richard Hynes, Eric Klinger-Wilensky, Casey Kobi, Travis Laster, Tom Lin, Steven Rosenblum, Rob Spatt, Andrew Tuch, participants at the fall 2013 Penn Law ILE Roundtable for their comments on earlier versions, and to our research assistants John Cooper, Nicholas Griffin, and Marisa Kirio.

** William B. Johnson Professor of Law & Economics; Co-Director, Institute for Law & Economics, University of Pennsylvania Law School.

reputation. The constraints of the reputational market emerge as more robust in consequence.

I. Introduction

On Valentine's Day 2011, Delaware's Vice-Chancellor Travis Laster enjoined the shareholder vote on a private equity buyout of Del Monte Foods Company. The ground: the company's board of directors was disabled from acting fairly in approving the merger due to the conflicted position of its investment banker–advisor, Barclays.[1] The injunction lasted only twenty days, and the deal eventually closed.[2] Even so, the ruling rocked the world of mergers and acquisitions (M&A)[3] by casting standard practices into question, most prominently "stapled" financing—an arrangement in which the selling company's banker–advisor also finances the purchase price for the buyer. Uncertainty followed for sell-side companies, their advisors, and their counsel.[4]

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1. *In re* Del Monte Foods Co. S'holders Litig., 25 A.3d 813, 839–40 (Del. Ch. 2011).

2. *Id.* at 840.

3. *See, e.g.*, Ashby Jones, *Him Again? Laster Rips Barclays, Holds up Del Monte Sale to PE Group*, WALL ST. J. L. BLOG (Feb. 15, 2011, 4:11 PM), http://blogs.wsj.com/law/2011/02/15/him-again-laster-rips-barclays-holds-up-del-monte-sale-to-pe-group, *archived at* http://perma.cc/4M9Z-AQWL (noting that the decision "casts a harsh light" on typical Wall Street bank M&A advisory practices).

4. *See* David Marcus, *The Case of J. Travis Laster*, DEAL PIPELINE (Apr. 1, 2011, 12:51 PM), http://pipeline.thedeal.com/tdd/ViewArticle.dl?id=10003542734, *archived at* http://perma.cc/MYQ5-Y3Z8 (discussing Vice-Chancellor Laster's boldness, the decision in *Del Monte*, and legal and financial professionals' concerns about the resulting lack of predictability in their work); Vipal Monga, *Make My Day*, DEAL PIPELINE (Feb. 18, 2011, 11:21 AM), http://pipeline.thedeal.com/tdd/ViewBlog.dl?id=38439, *archived at* http://perma.cc/R2YN-H6GZ ("Laster's opinion exposes the taken-for-granted process that occurs in many going-private deals."); Shira Ovide & Gina Chon, *Judge Delays KKR's Del Monte Deal and Slams Barclays*, WALL ST. J. DEAL J. (Feb. 15, 2011, 1:19 PM), http://blogs.wsj.com/deals/2011/02/15/judge-delays-kkrs-del-monte-deal-and-slams-barclays, *archived at* http://perma.cc/32SW-39PD (reporting on Vice-Chancellor Laster's criticism of Barclays for providing what many banks believe is "bread-and-butter" advisory work). Commentary continued for some time. *See, e.g.*, Robert Teitelman, *Strine, El Paso and the Shaming Thing*, DEAL PIPELINE (Mar. 7, 2012, 1:01 PM), http://www.thedeal.com/content/regulatory/strine-el-paso-and-the-shaming-thing.php, *archived at* http://perma.cc/ZC5X-VH72 (describing Vice-Chancellor Laster as suffering "considerable blowback").

A second upset followed just over a year later, when then-Chancellor Leo Strine ruled on a request to enjoin the shareholder vote on the merger of El Paso Corporation into Kinder Morgan, Inc.[5] Investment banker conflicts had poisoned the sell-side well once again and the court excoriated the actors responsible, in particular Goldman Sachs.[6] But this time the injunction was refused, the chancellor declining to obstruct sell-side shareholder access to what might be deemed a good deal.[7] Reaction again was loud. Some praised the chancellor's shaming strategy,[8] while others accused him of surrendering to the investment banking interest in declining to enjoin.[9] Still others thought that any surrender was to the plaintiffs' lawyers[10]: the chancellor had departed from "traditional principles of agency law."[11] It was a case of a judge making a mountain out of a Wall Street molehill.[12] There were even whispers about ulterior motives—many

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5. *In re* El Paso Corp. S'holder Litig., 41 A.3d 432, 433, 452 (Del. Ch. 2012).

6. *Id.* at 440–44.

7. The case was not closed, for the breaches of duty were left over for *ex post* litigation over liability and damages. *Id.* at 451–52.

8. *See* Reynolds Holding, *Judges' Words Can Speak as Loudly as Actions*, REUTERS BREAKINGVIEWS (Mar. 20, 2012), http://blogs.reuters.com/breakingviews/2012/03/20/judges-words-can-speak-as-loudly-as-actions, *archived at* http://perma.cc/JU7S-DUEY (describing strong, public shaming techniques like Chancellor Strine's as "useful precedent" in shaping behavior); Steven Davidoff Solomon, *The Losers in the El Paso Corp. Opinion*, DEALBOOK, N.Y. TIMES (Mar. 1, 2012, 1:20 PM), http://dealbook.nytimes.com/2012/03/01/the-losers-in-the-el-paso-corp-opinion/?, *archived at* http://perma.cc/U42H-RGAY (identifying seller CEO Douglas Foshee and the bank as the losers); Teitelman, *supra* note 4.

9. *See* David Weidner, *Is Leo Strine Serious?*, WALL ST. J., Mar. 8, 2012, http://online.wsj.com/article/SB10001424052970203961204577268191951502420.html, *archived at* http://perma.cc/8WPK-3UR2 (arguing that Chancellor Strine colorfully criticized the transaction but ultimately failed to provide a remedy for the shareholders); Stefan Padfield, *A Test Case for Shaming as Sanction?*, THERACETOTHEBOTTOM.ORG (Mar. 10, 2012, 11:26 AM), http://www.theracetothebottom.org/home/a-test-case-for-shaming-as-sanction.html, *archived at* http://perma.cc/R63Q-2VCG (expressing skepticism that the bankers from Goldman would face any real financial or reputational consequences following Chancellor Strine's decision to deny an injunction in *El Paso*); Brian J.M. Quinn, *Is Corporate Law Serious? Maybe . . . Maybe Not*, M&A L. PROF BLOG (Mar. 8, 2012), http://lawprofessors.typepad.com/mergers/2012/03/is-corporate-law-serious.html, *archived at* http://perma.cc/SD7G-EAAN (considering whether leaving decisions up to shareholders, as in the *El Paso* decision, represents a failure of corporate law); Jonathan Weil, *Goldman Raises Conflicts to a High Art*, BLOOMBERG VIEW (Mar. 8, 2012, 7:00 PM), http://www.bloomberg.com/news/2012-03-09/goldman-sachs-raises-conflicts-to-a-high-art-jonathan-weil.html, *archived at* http://perma.cc/TU9N-9JP3 (suggesting that bankers emerged as the real winner).

10. Alison Frankel, *How Plaintiffs' Lawyers Are Winning the Delaware Injunction Game*, ANALYSIS & OPINION, REUTERS (Mar. 7, 2012), http://blogs.reuters.com/alison-frankel/2012/03/07/how-plaintiffs-lawyers-are-winning-the-delaware-injunction-game/, *archived at* http://perma.cc/S3AM-JAGL (noting that filing for preliminary injunctions can help shareholders recover after-the-fact damages, which helps plaintiffs' lawyers recover fees).

11. Robert T. Miller, *Journeys in* Revlon-*Land with a Conflicted Financial Advisor:* Del Monte *and* El Paso 18 (Univ. of Iowa, Legal Studies Research Paper No. 12-24, 2012), *available at* http://ssrn.com/abs=2156488, *archived at* http://perma.cc/QP6T-J3A2.

12. *See* Matt Levine, *Delaware Judge Driven to Possibly Obscene Energy Industry*

see today's Delaware courts in an awkward institutional position, working to retain their leading position as corporate law arbiters even as plaintiffs increasingly choose other venues for litigation of Delaware corporate law claims.[13] Recent Chancery Court decisions can be seen as compensating tilts in the direction of the plaintiffs' bar[14] and these investment banker cases readily take the profile.[15]

Blowback continued a year later still. The Chancery Court's hard looks at Barclays and Goldman had come to be seen as game changers[16]: sell-side boards suddenly had become ultrasensitive to banker conflicts;[17] staples were said to have largely disappeared;[18] and big banks like Goldman

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Euphemism by Kinder-El Paso Merger, DEALBREAKER (Mar. 1, 2012, 6:47 PM), http://dealbreaker.com/2012/03/delaware-judge-driven-to-possibly-obscene-energy-industry-euphemism-by-kinder-el-paso-merger/, *archived at* http://perma.cc/XP2R-NTN6 ("Strine makes much of the fact that Morgan Stanley only got paid if the merger happened. Welcome to all mergers! That, by the way, is actually a real conflict. But it's hallowed by tradition so whatever."). Inconsistency between the cases' two results also was a topic of discussion. *See, e.g.*, Solomon, *supra* note 8 (recognizing that the decision of the chancellor in *El Paso* was a "different approach than the one adopted" in *Del Monte*).

13. A stack of scholarly studies confirms this. *See* Matthew D. Cain & Steven M. Davidoff, *A Great Game: The Dynamics of State Competition and Litigation*, 100 IOWA L. REV. (forthcoming 2014) (manuscript at 3, 5), *available at* http://ssrn.com/abstract=1984758, *archived at* http://perma.cc/JL94-WF78 (studying 1,117 M&A transactions greater than $100 million from 2005 to 2011 and finding that "Delaware attracts only 44.6% of [state merger] litigation"); Jennifer J. Johnson, *Securities Class Actions in State Court*, 80 U. CIN. L. REV. 349, 361, 369 (2011) (analyzing a dataset of state securities class action filings and finding that "while the number of Delaware securities class actions has increased, the relative percentage of Delaware cases compared to those in other jurisdictions has fallen"); Brian J.M. Quinn, *Shareholder Lawsuits, Status Quo Bias, and Adoption of the Exclusive Forum Provision*, 45 U.C. DAVIS L. REV. 137, 148 (2011) (studying a dataset of 119 mergers and showing that only 7% of mergers that involved litigation were filed solely in Delaware and 40% were filed solely outside of Delaware); John Armour et al., *Is Delaware Losing Its Cases?* 19–20 (Nw. Univ., Law & Econ. Research Paper No. 10-03, 2010), *available at* http://ssrn.com/abstract=1578404, *archived at* http://perma.cc/7KFZ-M8R8 (showing that Delaware courts have been receiving a declining share of suits relating to M&A, as "suits against Delaware targets have become increasingly common in both federal court and in other state courts").

14. *See, e.g.*, Ams. Mining Corp. v. Theriault, 51 A.3d 1213, 1252 (Del. 2012), *aff'g In re* S. Peru Copper Corp. S'holder Derivative Litig., 52 A.3d 761 (Del. Ch. 2011) (affirming a Delaware Chancery Court award of over $2 billion in damages and over $304 million in attorneys' fees); Alison Frankel, *Record $285 ML Fee Award is Strine's Message to Plaintiff's Bar*, ANALYSIS & OPINION, REUTERS (Dec. 21, 2011), http://blogs.reuters.com/alison-frankel/2011/12/21/record-285-ml-fee-award-is-strines-message-to-plaintiffs-bar/, *archived at* http://perma.cc/PYE2-RHHA (noting that Strine's opinion in *Southern Copper* indicated Delaware would continue to reward plaintiff's firms for bringing high-risk suits by ensuring they are "well compensated").

15. We note that any compensating tilts are in turn compensated by Chancery Court decisions that constrain plaintiffs' venue choices. *See, e.g.*, Boilermakers Local 154 Ret. Fund v. Chevron Corp., 73 A.3d 934, 963 (Del. Ch. 2013) (sustaining forum selection bylaws).

16. *See* Liz Hoffman, *Boutique Banks Ride Conflict Fears up M&A League Tables*, LAW360 (Apr. 3, 2013, 9:42 PM), http://www.law360.com/articles/429765/boutique-banks-ride-conflict-fears-up-m-a-league-tables, *archived at* http://perma.cc/VA6L-77RD (noting that the warnings in the Chancery Court's *Del Monte* and *El Paso* opinions had "seeped into deal making").

17. *Id.*

18. *Id.*

and Barclays were losing market share while smaller, conflict-free "boutique" advisory firms rose to the top ten league rankings.[19] The cases had so much affected transactional practice as to prompt talk of overkill,[20] with Delaware judges themselves commenting about possible deal maker overreaction.[21]

But the Chancery Court returned to the fray undaunted in 2014. In *In re Rural Metro Corp. Stockholders Litigation*,[22] Vice-Chancellor Laster ruled against a banker once more, this time after a trial on the merits, confirming the vitality of banker liability on an aiding and abetting theory.[23] Some commentators pushed back yet again, this time warning of crushing damages.[24] Others noted the opinion with approval.[25]

It seems the Chancery Court is damned if it doesn't and damned if it does when it comes to conflicted investment bankers. It is overly lenient and ineffectual in the eyes of some, while in other eyes it is too quick to condemn, a slight raise of the judicial eyebrow seemingly bringing great financial institutions to their knees. At the same time, both sides seem to agree that the hard looks at banker conflicts in *Del Monte*[26] and *El Paso*[27] herald a break with the past.

In fact there is no change in the terms of the law. *Del Monte* and *El Paso* apply longstanding principles without modifying them in any way. The break with the past lies in the very act of application.[28] Important

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19. *Id.*

20. Liz Hoffman, *Takeaways from Tulane, Where M&A Elite Rub Elbows*, LAW360 (Mar. 25, 2013, 8:57 PM), http://www.law360.com/articles/426325/takeaways-from-tulane-where-m-a-elite-rub-elbows, *archived at* http://perma.cc/J9YL-2FXN.

21. *Id.*

22. 88 A.3d 54 (Del. Ch. 2014).

23. *Id.* at 63.

24. *See, e.g.*, Steven Davidoff Solomon, *Ruling Highlights Unequal Treatment in Penalizing Corporate Wrongdoers*, DEALBOOK, N.Y. TIMES (Mar. 18, 2014, 6:45 PM), http://dealbook.nytimes.com/2014/03/18/ruling-highlights-unequal-treatment-in-penalizing-corporate-wrongdoers/?_php=true&_type=blogs&_r=0, *archived at* http://perma.cc/Y4B9-KWDR (warning of a potential $250 million judgment against an investment bank over a deal for only $5.1 million).

25. *See, e.g.*, Mark Roe, *The Examiners: Mark Roe on the Rural/Metro Ruling*, BANKRUPTCY BEAT, WALL ST. J. (May 2, 2014, 12:12 PM), http://blogs.wsj.com/bankruptcy/2014/05/02/the-examiners-mark-roe-on-the-ruralmetro-ruling/, *archived at* http://perma.cc/NC4L-LS9M (noting that the opinion was "a strong one, not to be criticized by anyone other than conflicted bankers").

26. *In re* Del Monte Foods Co. S'holders Litig., 25 A.3d 813 (Del. Ch. 2011).

27. *In re* El Paso Corp. S'holder Litig., 41 A.3d 432 (Del. Ch. 2012).

28. History holds out only one comparable *Revlon* case: Mills Acquisition Co. v. Macmillan, Inc., 559 A.2d 1261 (Del. 1988). The facts were so extreme as to make it distinguishable. The top executives at Macmillan were attempting to execute a management buyout with KKR. *Id.* at 1264. Since their deal contemplated that they would remain with the company after the merger, the transaction was scrutinized under the duty of loyalty as a self-dealing transaction as well as under *Revlon*. *Id.* at 1280. A rival bidder, Maxwell, complicated things for the executives. As the auction proceeded they tipped their own favored bidder, KKR, about Maxwell's moves. *Id.* at 1275. Macmillan's investment banker, Bruce Wasserstein, fell in with the favoritism, funneling information to KKR that was not shared with Maxwell, *id.* at 1276, and later falsely representing

questions arise in consequence, questions about the relationship between banker–advisors and their corporate clients, questions often asked in the past but never satisfactorily answered. Is this a fiduciary relationship? If the answer is yes, why should banker conflicts be tolerated at all in a world where nobody would proceed with a sale process where the same law firm represented both sides? If banker conflicts jeopardize the interests of sell-side shareholders, it would seem to follow that bankers should be modeled like lawyers and accountants—as professionals whose ethical responsibilities include conflict avoidance. Alternatively, perhaps the relationship is not fiduciary, and if it is not, why should investment banker conflicts have a disabling effect on the good faith actions of independent sell-side directors? If professionalization is unsuited to the bankers' role, then conflicts should be expected and arguably tolerated. Which doctrinal template comes to bear here, fiduciary or contract?

This Article answers these questions, offering the first sustained look at the banker–client advisory relationship in this country's legal literature.[29] We take the two basic legal building blocks—the agency law that channels the banker's relationship with its client and the *Revlon*[30] doctrine that inspects the client's diligence in selling the company—and frame the issues contextually, looking to M&A practice, the structure of the advisory sector, and applicable economic theory, making a further comparative reference to the conflict-of-interest rules governing the lawyers and auditors who also provide services to large corporate clients.

A clear answer to the questions emerges: although this is nominally fiduciary territory, both banker–client relationships and the Chancery

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to the board that the auction had been fairly conducted. *Id.* at 1277. Applying the rule under the duty of loyalty, the court required that the process must pass entire fairness review. *Id.* at 1280. The court found no justification for the misinformation and discrimination against Macmillan. *Id.* at 1281–82. The banker's failure to disclose the KKR tip to the board was also disabling—when a board is deceived by self-interested actors, it ruled, board decisions are "voidable at the behest of innocent parties to whom a fiduciary duty was owed and breached." *Id.* at 1284.

29. Professor Tuch offers an extensive review of banker–client relationships in Australian law. *See* Andrew Tuch, *Investment Banks as Fiduciaries: Implications for Conflicts of Interest*, 29 MELB. U. L. REV. 478, 479–80 (2005) [hereinafter Tuch, *Investment Banks*] (discussing whether banker–client relationships give rise to a fiduciary duty under Australian law); Andrew Tuch, *Obligations of Financial Advisors in Change-of-Control Transactions: Fiduciary and Other Questions*, 24 COMPANY & SEC. L.J. 488, 489 (2006) (considering whether Australian law compels bankers to avoid conflicts of interest in change-of-control transactions or if "less onerous" conflict-management procedures are sufficient); Andrew Tuch, *The Paradox of Financial Services Regulation: Preserving Client Expectations of Loyalty in an Industry Rife with Conflicts of Interest* 2–3, 15 (Sydney Law Sch., Legal Studies Research Paper No. 08/21, 2008) [hereinafter Tuch, *Paradox*], *available at* http://ssrn.com/abstract=1086480, *archived at* http://perma.cc/4LCH-FEE3 (highlighting the types of conflicts that inherently arise due to the organizational structure of modern investment banks and examining statutory obligations to manage such conflicts under Australian law). Tuch answers the question regarding the application of fiduciary duty affirmatively, analogizing to a number of other relationships under various countries' laws. Tuch, *Investment Banks*, *supra*, at 490–97.

30. Revlon, Inc. v. MacAndrews & Forbes Holdings, Inc., 506 A.2d 173 (Del. 1986).

Court's recent interventions are contractually driven. Banker–advisors are agents and therefore fiduciaries, but they and their clients also make full use of agency law's opt-out permission, opening a wide door to permit conflicted representation. Corporate law lends a hand by cutting off shareholder actions in respect of the agency. Conflicts of interest have become wrought into banker–client relationships; as a result, the structure of the advisory sector makes them hard to avoid and clients, expecting them, make allowances. Advisor banks emerge in practice as arm's-length counterparties constrained less by rules of law than by a market for reputation. The corporate lawyers who work beside the bankers on the same deals make for an interesting contrast: although the legal regime governing lawyer conflicts is not fundamentally different, reputational constraints loom much larger and conflicts are more likely to be avoided.

Meanwhile, the boards of directors that engage bankers clearly *are* fiduciaries in law and fact, and company sales processes implicate enhanced scrutiny of their performance under *Revlon*.[31] *Revlon* scrutiny, however, is not in the first instance about traditional fiduciary self-abnegation. It is instead about diligence in getting the best deal for the shareholders. *Revlon* review takes the court through all aspects of the deal, both the contract itself and the process that creates it.[32] Anything that impairs sell-side incentives is a fair topic for questioning, including banker conflicts.

Del Monte and *El Paso* stand for the proposition that sell-side boards must treat banker contracts in a contractual rather than fiduciary frame. The cases presuppose that bankers and clients have opted to define their relationships contractually and proceed to work out this choice's logical implications in the context of review of the selling board's diligence. Contract follows on contract: a client with a *Revlon* duty has no business consenting to a conflict and then passively trusting that the conflicted fiduciary will deal in the best of faith. The client should instead treat the banker like an arm's-length counterparty, assuming self-interested motivation on the banker's part and using contract to protect itself and its shareholders. Although one can draw a clash of fiduciary and contractual values out of the cases' facts, as a structural matter—both economic and doctrinal—the cases are about taking contract seriously. They show us fiduciary principles operating at a high stage of evolution tailored to the sophisticated context of M&A.

This contractual perspective further explicates the cases' impact. They certainly usher in a stricter regime of conflict management in sell-side boardrooms. But they also usher in the Delaware Chancery Court itself as a

31. *Id.* at 179, 182 (requiring directors to maximize short-term value once they have decided to sell a company for cash).

32. *See id.* at 176 (holding that Delaware law did not permit lock-up agreements if the contracts resulted from a process that was tainted by a breach of fiduciary duty).

focal-point player in the market for banker reputation. The court's fact-finding uncovers hidden information about banker conduct, prompting reputational reassessment. An accompanying negative legal judgment makes the court's interventions doubly unwelcome to the bankers. This is unsurprising, for reputational market constraints emerge as more robust.

Having answered the questions about the cases' legal and normative implications, undercutting the notion that *Del Monte* and *El Paso* impose traditional fiduciary norms on unwilling, sophisticated parties, we turn to the cases' critics and their claims that they do too little to police banker conflicts or, alternatively, too much. We test the Chancery Court's approach of case-by-case intervention under the open-ended *Revlon* standard to the closest available alternatives. We play both sides, asking whether bankers plausibly can be treated either as professionals owing strict fiduciary duties or contract counterparties free to pursue self-interested goals. The inquiry leads to two thought experiments: we consider each of per se prohibition of banker conflicts and safe harbors that make them less vulnerable to challenge. Neither of these clearer alternatives proves feasible or superior. Conflicted bankers, if appropriately managed, can add value to a deal; conflicted bankers, if not appropriately managed, can be a destructive influence even given full disclosure and engagement of a second, unconflicted banker.

We are left launching actors in the M&A world into a rough, litigious sea of uncertainty. But they can navigate it. The primary decision makers here are not courts but independent directors of selling companies, actors with recourse to the best available legal counsel. As such, they are well equipped to make adjustments and cope with banker conflicts in the wake of these Chancery Court interventions. The practice has indeed changed. Stapled financing persists, but not in acquisitions likely to trigger *Revlon* scrutiny. Conflicts remain wrought into banker–client relationships even so. And, while relatively less conflicted boutique investment banks have gained some market share since 2011,[33] they have done so in continuance of a trend going back many years.[34]

Part II looks at what investment bankers do when companies are sold. It first describes the merger-advisory role, in which the banker is the channel for the board's information about both a sale's desirability and the optimal set of terms. Part II goes on to detail two ancillary services, the rendering of fairness opinions and the provision of debt financing.

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33. David Gelles, *30% of M.&A. Advisory Fees Went to Smaller Firms in 2013*, DEALBOOK, N.Y. TIMES (Jan. 8, 2014, 2:56 PM), http://dealbook.nytimes.com/2014/01/08/a-banner-year-for-boutique-investment-banks/, *archived at* http://perma.cc/UM5S-X9TS.

34. Paul Sharma, *Investment Banking Goes Boutique*, WALL ST. J., Oct. 10, 2010, http://online.wsj.com/news/articles/SB10001424052748704657304575539952433801886, *archived at* http://perma.cc/6EQC-JWET (demonstrating that boutique investment firms' market share gains are part of an existing trend).

Conflicts prove pervasive. Bankers often have ties to acquiring companies and the parties financing their deals, leading to incentives to cater to the other side of the negotiating table. An all-or-nothing success fee gives the banker an incentive to push for any deal at the expense of a good deal. And, as commercial banks have acquired investment banks in the wake of deregulation, sell-side advisors have started showing up as buy-side lenders, importing an added incentive to get the deal closed on the buyer's terms. As the incentive problems are laid out for inspection, it becomes clear that compromised advisors can distort sales processes, injuring sell-side shareholders.

Part III takes a closer look at these conflicts of interest, bringing two frameworks to bear. We first apply economic analysis, which looks toward contractual solutions to problems created by conflicts, primarily price adjustments and reputational constraints on conflicted parties. It also strongly counsels against per se prohibition. We then look at the legal framework, showing that bankers, as agents, owe fiduciary duties to their corporate principals, but with an opening for client consent to agent conflicts—an opening subject to a process rule of backstop, rule of full disclosure, and an overarching requirement of good faith. The law synchronizes neatly with both the relational picture highlighted in the economic analysis and the terms of banker–client engagement contracts. All frameworks converge on the same conclusion: in this relationship, market-based transactions trump traditional fiduciary values and regulatory constraints stem from markets for reputation rather than from bright-line legal rules.

Part IV turns to the hard looks in *Del Monte* and *El Paso*. The cases situate the conflicts problem at a front-and-center spot on the transactional stage, upping the stakes. This follows not from a change in the law but from the facts. The bankers in these cases play the primary advisory role rather than the secondary role of fairness-opinion giver, the role on which the case law has focused heretofore.[35] When a conflict compromises the banker's performance in the primary role of negotiating the deal, *Revlon* questions follow.

Del Monte and *El Paso* raise a difficult law-to-fact issue: whether a *Revlon* violation based on a banker conflict can follow from a showing of an incentive impairment—a "taint" taken alone—or requires a stronger showing of realized negative consequences for the sale process. Our analysis identifies consequences of a "might have been," counterfactual nature in both cases, but also highlights room for argument. *El Paso* is

35. Steven M. Davidoff, *Fairness Opinions*, 55 AM. U. L. REV. 1557, 1560–61 (2006) (noting that after a period of criticism in the 1990s, "Delaware courts continued to place persuasive reliance on fairness opinions").

particularly susceptible to a reading of per se actionability, even as the conflict in question in the case was particularly severe.

The results can be seen to follow from an application of strong fiduciary norms. But we think such a reading misses the point. The Chancery Court takes a relentlessly contractual approach here. To make a taint actionable under *Revlon* is not to slam down an ethical rule. It instead embodies a determination that a banker's incentives undermined a contracting process—an economic judgment with legal consequences.

In Part V we address both those who criticize the Chancery Court for lax treatment and those who describe the cases as fiduciary overkill. At the same time, we ask whether it is feasible to substitute a rule-based approach to banker conflicts, importing certainty to actors in the marketplace. We experiment with two alternative regimes, one stricter and the other more accommodating, both rule based. The stricter approach is per se prohibition of conflicts, posed by analogy to the law governing auditor–client relationships. We show that full prohibition could create as many problems as it solves and in any event is institutionally unsuitable as an outgrowth of *Revlon* review. We then look into an alternative: a narrow prohibition directed only to stapled financing. This proves more robust institutionally but still fails the substantive test: staples are not intrinsically inimical to the shareholder interest. We then turn to a more accommodating approach—a safe harbor for banker conflicts conditioned on full disclosure and engagement of a second, unconflicted banker. We show that the combination has a cleansing effect but not enough of an assurance to guarantee the integrity of the *Revlon* regime.

A conclusion follows.

II. The Business Side

The dispute between investment bankers and Delaware chancellors concerns the bankers' performance as advisors to the boards of selling companies. A cogent evaluation of the dispute's particulars requires contextual grounding. We accordingly preface our legal analysis with a look at the business side. Subpart A focuses on what bankers do, first describing their central advisory function and going on to two ancillary services, provision of fairness opinions and financing. In subpart B we go on to look at the incentive structure of the banker–client relationship, detailing conflicts of interest that potentially skew the performance of the advisory role to the detriment of the interests of target shareholders.

A. Services Rendered

1. Advising on Partner, Price, and Process.—The senior management suite of an operating company is unlikely to be populated with M&A experts. The company's board of directors accordingly needs outside help when another company proposes a merger or the company's managers themselves inquire into sale possibilities.[36] Either way, the board calls on an investment banker for expert advice about market conditions and alternative modes of sale.[37] Indeed, sale processes often originate in the suggestion of a banker looking to drum up advisory business.[38]

Transaction planning has only just begun with an affirmative answer to the question as to "whether" to sell. There follows a series of further questions with significant value consequences. There can be a "what" question: if the company has multiple divisions, sale of a piece or pieces might yield more than sale of the whole. Then come "how" and "to whom." An open auction might or might not yield more than a process focused on a bilateral negotiation with a single acquirer. A transaction with an operating company in the same line of business (a strategic merger) might or might not yield more than a private equity buyout (a financial merger). Negotiation with a given suitor involves further choices regarding sale process, mode of payment, and the merger agreement's ancillary terms. At the bottom line looms an overarching "how much" question.

The bank helps management answer all the questions, bringing its expertise to bear.[39] Its participation in the sale process starts with a valuation of the selling company, an analysis that provides a basis against which to evaluate the attractiveness of subsequent offers.[40] The valuation also figures into the marketing effort, as the banker works with management to project a promising future performance by the company.[41] The bank then searches for potential bidders, drawing on its knowledge of the target's industry to identify companies whose lines of business hold out

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36. *Cf.* Henri Servaes & Marc Zenner, *The Role of Investment Banks in Acquisitions*, 9 REV. FIN. STUD. 787, 806 (1996) (explaining that companies look outside for advisors in more complex transactions).

37. *See id.* (highlighting the fact that a firm may rely on an investment bank when the firm does not have the needed expertise).

38. J. Peter Williamson, *Mergers and Acquisitions*, *in* INVESTMENT BANKING HANDBOOK 219, 226–27 (J. Peter Williamson ed., 1988).

39. Alan Morrison and William Wilhelm describe the skills bankers bring to bear as follows:

> [T]he central investment bank activity is the creation of private law in situations where the precise quantification of the parameters of trade is impossible, either as a consequence of their extreme complexity, or because it would involve the disclosure of facts that would undermine the value of the exchange. The skills needed to fulfill this role are hard to pass on at arm's length: they are best learned through day-to-day contact with an expert mentor and once learned, they cannot easily be codified and widely disseminated at arm's length. This type of skill was characterized by Polanyi . . . as *tacit*.

ALAN D. MORRISON & WILLIAM J. WILHELM, JR., INVESTMENT BANKING: INSTITUTIONS, POLITICS, AND LAW 265 (2007).

40. *See* Anup Agrawal et al., *Common Advisors in Mergers and Acquisitions: Determinants and Consequences*, 56 J.L. & ECON. 691, 697 (2013) (listing target valuation as a service provided by investment banks).

41. *Id.*

an appropriate fit. Absent a fit, the banker looks for a buyer to which the target makes sense as a diversification play or, alternatively, for a financial purchaser.[42] The banker compiles a list of potential bidders, dividing them into strategic and financial categories.[43]

Decisions also need to be made about the sale process. Alternatives fall along a range: at one extreme comes a negotiated transaction on an exclusive basis with a single prospect; at the other extreme comes an auction open to all potential purchasers; in between come controlled auction processes centered on bilateral negotiations with multiple suitors.[44] Whatever the choice, the bank is heavily involved in negotiations with potential acquirers.[45]

By way of example, consider the sequence of moves in a controlled auction. The banker circulates a description of an unnamed target.[46] Companies interested in bidding sign confidentiality agreements before getting access to a detailed offering memorandum prepared by the bank.[47] The bank also will facilitate the due diligence processes of serious bidders.[48] Subsequent discussions, which can go forward with more than one bidder, focus on an emerging merger agreement, drafted by counsel with the bank's assistance.[49] The agreement contains terms on price and transaction structure along with several other terms with high value salience: a material-adverse-change clause setting conditions permitting the buyer to exit, a fiduciary out permitting the target to exit in the wake of a higher bid, and a breakup fee to be paid by the target in the event of its exit.[50] Final bids are submitted with the merger agreement on the table.[51] Given a successful bid, the merger agreement is submitted for the approval of the constituent boards of directors.[52] Given board approval, the last step is approval by a majority vote of the target shareholders,[53] with the bank joining counsel in preparing the proxy statement.[54]

The advisory bank is retained and paid pursuant to an engagement letter.[55] Typical advisory fee arrangements include a retainer and a

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42. WILLIAMSON, *supra* note 38, at 233.

43. GIULIANO IANNOTTA, INVESTMENT BANKING: A GUIDE TO UNDERWRITING AND ADVISORY SERVICES 122 (2010).

44. *Id.* at 122–23.

45. Agrawal et al., *supra* note 40, at 697–98.

46. IANNOTTA, *supra* note 43, at 123.

47. *Id.*

48. Agrawal et al., *supra* note 40, at 697.

49. IANNOTTA, *supra* note 43, at 125; Agrawal, *supra* note 40, at 697.

50. IANNOTTA, *supra* note 43, at 125.

51. *Id.*

52. DEL. CODE ANN. tit. 8, § 251(b) (2011).

53. *Id.* § 251(c).

54. Agrawal et al., *supra* note 40, at 697.

55. Charles W. Calomiris & Donna M. Hitscherich, *Banker Fees and Acquisition Premia for*

"success fee"[56] pegged at a small percentage of the purchase price.[57] On average, around 80% of fees bankers draw from M&A depend on the deals' successful completion.[58]

2. Opining on Price.—In addition to advising on transactional choices, investment bankers formally opine on the fairness of the price—approximately 80% of target boards and 37% of acquirer boards procure such an opinion.[59] The opinion is addressed to the retaining board, which in turn relies on the opinion when approving the merger. Literally, the opinion states that the price is "fair" from a "financial point of view."[60] These are, however, terms of art with tightly circumscribed meanings: the statement confirms only that the price lies within a range of intrinsic values, any of which could be fair.[61] Accordingly, a fair price is not necessarily a best or even a good price.[62] Moreover, the opinion does not define what makes the numbers on the range of intrinsic values the fair set.[63] Nor does the opinion make a recommendation regarding acceptance or rejection of the merger.[64]

Fairness opinions do set out the valuation metrics used in establishing the price range. The bank chooses among a menu of possibilities[65]—discounted cash flow, comparable companies, comparable sale premiums,

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Targets in Cash Tender Offers: Challenges to the Popular Wisdom on Banker Conflicts 3 (Nat'l Bureau of Econ. Research, Working Paper No. 11333, 2005), *available at* http://www.nber.org/papers/w11333, *archived at* http://perma.cc/PTP8-XSD7.

56. Success fees come in three forms: (1) a constant percentage of the purchase price; (2) a constant dollar amount payable only on the contingency's occurrence; and (3) a rising sliding scale based on the amount of the purchase price. *Id.* at 6.

57. The fee is typically 1%, with the percentage declining as transaction size increases. Agrawal et al., *supra* note 40, at 694.

58. *Id.*

59. Darren J. Kisgen et al., *Are Fairness Opinions Fair? The Case of Mergers and Acquisitions*, 91 J. FIN. ECON. 179, 179 (2009); *cf.* Matthew D. Cain & David J. Denis, *Information Production by Investment Banks: Evidence from Fairness Opinions*, 56 J.L. & ECON. 245, 246–47 (2013) (finding that with a smaller sample, 96% of target boards procure a fairness opinion). Cain and Denis show that these acquiring boards tend to solicit fairness opinions in cases where the merger must be submitted for their shareholders' approval. In their sample only 28% of acquirers solicited an opinion, but 83% did so in cases of joint proxy solicitation. *Id.* at 254–55.

60. Cain & Denis, *supra* note 59, at 249.

61. *Id.*

62. *Id.*

63. Fair value could mean any one of a number of things—the company's stand-alone value without reference to a sale, the yield expected in an open auction of the company, the yield from an arm's-length sale of the company, or something else. Lucian Ayre Bebchuk & Marcel Kahan, *Fairness Opinions: How Fair Are They and What Can Be Done About It?*, 1989 DUKE L.J. 27, 30–32.

64. Calomiris & Hitscherich, *supra* note 55, at 4. Nor does the opinion purport to verify the information base relied on in its analysis, which comes from management. *Id.*

65. Bebchuk & Kahan, *supra* note 63, at 36–37.

or a weighted average of results from more than one approach.[66] The bank also is free to project different sale scenarios—a sale of the whole, a sale of separate pieces, a liquidation, or a weighted average of more than one.[67] The final document, in sum, results from discretionary choices, its conclusion amounting to the banker's subjective opinion based on market parameters.[68]

A fairness opinion may implicate a separate, fixed fee.[69] Assuming that the board's banker–advisor renders the opinion, the rule of thumb ratio between the amount of the banker's success fee and the amount paid for the opinion is ten-to-one.[70] Significantly, nothing requires the selling board to rely on its advisor for the opinion, although so doing yields obvious economies of scope and is the usual practice.[71] The board can engage a different bank for the opinion, paying it a fixed fee.[72] Alternatively, opinions can be solicited from the advisor and one or more other banks, but that happens only in a minority of cases.[73] In around 80% of the cases in which the selling board seeks an opinion, it procures a single opinion from its banker–advisor.[74]

Such is the practice.[75] As we have seen, the banker–advisor's expertise and judgment figure importantly in the sale effort's success.

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66. Davidoff, *supra* note 35, at 1574–75.

67. *Id.* at 1574 & nn.73–77.

68. *Id.* at 1573–75.

69. Bebchuk & Kahan, *supra* note 63, at 38; Davidoff, *supra* note 35, 1586–87. Fixed fees come in two forms: (1) a retainer paid upon execution and delivery of the engagement letter or in installments during the term of the engagement and (2) a fee paid upon submission of a fairness opinion. Calomiris & Hitscherich, *supra* note 55, at 5–6.

70. Steven J. Cleveland, *An Economic and Behavioral Analysis of Investment Bankers When Delivering Fairness Opinions*, 58 ALA. L. REV. 299, 314 (2006); John S. Rubenstein, Note, *Merger & Acquisition Fairness Opinions: A Critical Look at Judicial Extensions of Liability to Investment Banks*, 93 GEO. L.J. 1723, 1727 (2005).

71. Kisgen et al., *supra* note 59, at 183.

72. *Id.*

73. *Id.* at 180, 199.

74. The percentage in the text is an extrapolation from numbers reported in Kisgen et al., *supra* note 59, at 186–87. Cain & Denis, *supra* note 59, at 254, report that in their sample 96% of targets procured at least one fairness opinion, 8% procured two, and 1% procured three.

75. We note that the Code of Ethics and Standards of Practice for the National Association of Realtors does not ask for much more. Under Standard of Practice 11-1, valuation opinions must contain ten minimum terms:

> (1) identification of the subject property
>
> (2) date prepared
>
> (3) defined value or price
>
> (4) limiting conditions, including statements of purpose(s) and intended user(s)
>
> (5) any present or contemplated interest, including the possibility of representing the seller/landlord or buyers/tenants
>
> (6) basis for the opinion, including applicable market data
>
> (7) if the opinion is not an appraisal, a statement to that effect

From a business perspective, the fairness opinion contributes little extra. Empirical studies search in vain for value added for sell-side shareholders stemming from fairness opinions. The studies find that fairness opinions do not significantly affect either the merger premium or returns on the target company's stock upon the merger's announcement.[76] Nor do fairness opinions make deal completion more likely,[77] although they do add to the base of publicly available information about the value of the target.[78]

Their primary function is legal defense. Investment bankers first figured into the law of M&A in the wake of the Delaware Supreme Court's 1984 decision of *Smith v. Van Gorkom*,[79] the case that famously found a sell-side board of directors liable for a breach of the duty of care.[80] The defendant board's defalcation lay in an inadequate informational base, and the absence of an investment banker fairness opinion on the merger price lay at the core of the empty informational set.[81] Fairness opinions have ever since amounted to a de facto mandate for diligent sell-side boards.[82] The opinion serves two defensive purposes. First, it provides evidence that the selling board informed itself of the intrinsic value of the company's equity. Second, it lays groundwork for an affirmative defense under Delaware's corporate code, which provides that directors are protected when "relying in good faith" on opinions provided by outside experts.[83]

> (8) disclosure of whether and when a physical inspection of the property's exterior was conducted
>
> (9) disclosure of whether and when a physical inspection of the property's interior was conducted
>
> (10) disclosure of whether the REALTOR® has any conflicts of interest

CODE OF ETHICS AND STANDARDS OF PRACTICE OF THE NATIONAL ASSOCIATION OF REALTORS § 11-1 (2014), *available at* http://www.realtor.org/sites/default/files/publications/2014/Policy/2014-Code-of-Ethics.pdf, *archived at* http://perma.cc/P64E-3B3B.

76. Kisgen et al., *supra* note 59, at 180. *But cf.* Steven M. Davidoff et al., *Fairness Opinions in M&As*, *in* THE ART OF CAPITAL RESTRUCTURING: CREATING SHAREHOLDER VALUE THROUGH MERGERS AND ACQUISITIONS 483, 491 (H. Kent Baker & Halil Kiymaz eds., 2011).

77. Kisgen et al., *supra* note 59, at 180.

78. Cain & Denis, *supra* note 59, at 248. The authors also find a correlation between stock returns around the proxy mailing date and the valuations in the target fairness opinion. *Id.*

79. 488 A.2d 858 (Del. 1985).

80. *Id.* at 890–93.

81. *Id.* at 881.

82. *See* William J. Carney, *Fairness Opinions: How Fair Are They and Why We Should Do Nothing About It*, 70 WASH. U. L.Q. 523, 527 (1992) (describing the *Van Gorkom* case as the "Investment Bankers' Civil Relief Act of 1985"); Daniel R. Fischel, *The Business Judgment Rule and the* Trans Union *Case*, 40 BUS. LAW. 1437, 1453 (1985) (noting that the most immediate effect of the *Van Gorkam* case was that "no firm considering a fundamental corporate change will do so without obtaining a fairness letter").

83. DEL. CODE ANN. tit. 8, § 141(e) (2011); *cf. Van Gorkom*, 488 A.2d at 875 (rejecting the defense when the directors relied on uninformed and inadequate opinions of the company's CEO and CFO).

Fairness opinions serve these defensive objectives well,[84] providing potent if not complete evidence of the sell-side board's fulfillment of its duty of care.[85]

3. Providing Financing.—Strictly speaking, service as a merger advisor and provision of a fairness opinion require appropriate expertise and access to information, capabilities within the competence of small, boutique investment banks.[86] Boutiques with specialties in a given industry tend to thrive when the industry undergoes a wave of concentration by merger.[87] Still, size has advantages and larger banks bring more to the table. A merger advisor from a large bank can look to the bank's other departments for informational assistance. The bank's securities analysts can suggest potential merger partners.[88] The market arbitrage desk can assist in accounting for fluctuations in the advisory client's stock price during the sale process.[89] Risk arbitrageurs and traders can project the market's reactions to different merger consideration packages.[90] Corporate finance departments can assist with debt-financing proposals.[91]

Now let us switch to the buy side. Larger banks advising acquirers have the wherewithal to assist directly with financing, underwriting new issues of securities, or directly lending funds. Of course, nothing forces an acquirer to engage its merger adviser to provide these services. But the coupling is quite common when underwriting is called for—according to one study the acquirer's advisor does the underwriting in 56% of acquisitions involving new issues of securities.[92] The claimed benefits are

84. Critics charge that the opinions fall short on the question of greatest concern to the selling shareholders, providing little assurance on the quality of the deal. *See* Dean Roger Dennis & Dennis R. Honabach, *Corporate Governance Theory in the 1990's*, 44 RUTGERS L. REV. 533, 549 (1992) ("By and large, the [fairness] reports are brief, boilerplated documents . . . ."). We do not find the criticisms well-taken. *See infra* note 193.

85. *See, e.g.*, In re Compucom Sys., Inc. Stockholders Litig., No. Civ.A. 499-N, 2005 WL 2481325, at *7 (Del. Ch. Sept. 29, 2005) (finding that a board of directors fulfilled their fiduciary duty of care, in part, by relying on fairness opinions); Crescent/Mach I Partners, L.P. v. Turner, 846 A.2d 963, 985 (Del. Ch. 2000) (rejecting the argument that approval of a fairness opinion potentially tainted by the advisor's conflict of interest deprived defendant directors of the section 141(e) defense).

86. For an account of the evolution of large, complex banks and the consequential appearance of small boutiques, see generally MORRISON & WILHELM, *supra* note 39, at 294–305. They note that size has costs as well as advantages, because it debilitates peer-group monitoring and detaches the professional's interest in his or her own human capital from the reputation of the firm, enervating incentives. *Id.* at 301. For a discussion of the boutique model and its effect on conflicts, see *infra* notes 147–56 and accompanying text.

87. Williamson, *supra* note 38, at 227–28.

88. *Id.* at 225.

89. *Id.* at 225–26.

90. *Id.*

91. *Id.* at 226.

92. Mine Ertugrul & Karthik Kirshnan, *Investment Banks in Dual Roles: Acquirer M&A*

expedited closing and economies of scope in the form of a reduced advisory fee.[93]

Traditionally, underwriting is a core line of business of U.S. investment banks.[94] In contrast, lending was long prohibited by the Glass-Steagall Act,[95] repealed in 1999.[96] As regulatory barriers fell, commercial banks acquired traditional investment banks, resulting in "universal" banks combining commercial banking and lending with functions previously the province of investment banks, including underwriting.[97] Such a banker–advisor can facilitate an acquirer's deal as a lender. But, for present purposes, a different coupling is more salient: as universal banks emerged, merger-advisory services on the *sell side* became coupled with purchase money lending to the *buy side*, so-called stapled financing.[98]

Staples first appeared as part of a larger package deal: the selling corporation puts itself (or a piece of itself) up for auction and offers debt financing to potential purchasers in tandem with the sale—financing to be supplied by the seller's banker–advisor.[99] The financing package is thus "stapled" to the offering memorandum.[100] The impetus for these couplings came from the banks themselves, which held out their lending capacity to lure potential selling companies into accepting their advisory services.[101] Over time, the term "staple" has come to be used more loosely, applying in any case where the seller's banker–advisor participates in financing the buyer's purchase.[102] We will follow the broader usage, noting differences of transactional context as we go.

The best case for stapled financing lies with the original auction structure. To frame the case, assume that a corporation is selling one of a number of divisions in a favorable credit market. Opening the door for bids on the division with a financing offer already on the table arguably makes

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Advisors as Underwriters, 37 J. FIN. RES. 139, 168 (2014).

93. *Id.* at 179.

94. Arthur E. Wilmarth, Jr., *The Transformation of the U.S. Financial Services Industry, 1975-2000: Competition, Consolidation, and Increased Risks*, 2002 U. ILL. L. REV. 215, 321.

95. Banking Act of 1933, Pub. L. No. 73-66, §§ 16, 20–21, 32, 48 Stat. 162, 184–85, 188–89, 194 (codified as amended in scattered sections of 12 U.S.C.) (repealed 1999) (restricting commercial banks, from among other things, engaging principally in investment banking activities).

96. Gramm-Leach-Bliley Act, Pub. L. No. 106-102, § 101, 113 Stat. 1338, 1341 (1999).

97. Wilmarth, *supra* note 94, at 319–20.

98. Davidoff, *supra* note 35, at 1588.

99. *Id.*

100. Richard Hall, *Stapled Finance Packages Under Scrutiny*, IFLR (Apr. 1, 2006), http://www.iflr.com/Article/1984558/Stapled-finance-packages-under-scrutiny.html, *archived at* http://perma.cc/TG4E-2PS5.

101. *Id.*

102. For example, the term would be used to describe an investment banking firm's offer to provide buy-side financing, as described in *In re Toys "R" Us, Inc. S'holder Litig*., 877 A.2d 975, 1005–06 (Del. Ch. 2005).

the deal more attractive despite the ready availability of credit—assured financing lowers the bidders' transaction costs so that more bidders show up.[103] As the stock of the division up for sale is not publicly traded, the bank's financing offer also facilitates establishment of a price floor for bidding: the bidders take the amount of financing on offer and work backward using projected leverage ratios.[104] The bank's presence could also attract private equity bidders to compete with a strategic acquirer and, in so doing, push the strategic bidder to a higher price.[105] Finally, the financing package provides a base point for competing financing offers by other banks.[106] If the stapled bank emerges in the lead, time to closing is reduced because the lender's diligence process already is underway.[107]

The above scenario assumes that credit flows freely, leading to competition among financing banks as well as bidders. The assumption does not diminish the case favoring staples, for it shows off the coupling's advantages even though competition among banks removes any doubt about the availability of financing. Presumably, the case for a staple strengthens further when credit is scarce; lining up the bank at stage one imports beneficial certainty. Other downside scenarios further expand the case for having the bank on both sides of the deal. For example, if credit tightens after the deal is signed but before closing, the sell-side fee yield could induce the bank to stay with the deal rather than exploring opportunities for exit.[108]

Now compare a case where a publicly traded company puts itself up for sale, indifferent as between a strategic or financial purchaser. A financial bidder emerges as the sale process unfolds and the seller's banker–advisor takes a place among the banks providing debt financing to the private equity buyer. This is also a staple under the broad usage. But,

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103. *See* Jeffrey E. Ross et al., Del Monte*: Staple Remover?*, 12 DEBEVOISE & PLIMPTON PRIVATE EQUITY REP. 1, 17 (2011) (explaining that stapled financing may attract more buyers by reducing the costs associated with securing financing on one's own).

104. *Id.* Note that the price-floor function matters more when the company being sold is not publicly traded, as would be the case when a private equity firm sells one of its portfolio companies or a publicly traded operating company sells a division. Note also that the price-floor argument can be turned around. The amount of financing on offer tips potential bidders to the advisor bank's hidden views on the value of the selling company. IANNOTTA, *supra* note 43, at 124. The staple's availability also can give rise to a negative inference: if the advisor bank is *not* participating in financing then the selling company is worth less than advertised. *Id.*

105. *See* Christopher Foulds, *My Banker's Conflicted and I Couldn't Be Happier: The Curious Durability of Staple Financing*, 34 DEL. J. CORP. L. 519, 528 (2009) (recognizing that stapled financing packages encourage competition between strategic buyers and financial buyers).

106. Ross et al., *supra* note 103, at 17. Presumably, if multiple bidders and banks are attracted, the staple becomes less and less relevant as the process continues. Compare a case where a seller requires the bidders to accept the staple. The element of coercion detracts from the case. But even here there is an argument: the staple reduces variability and makes it easier to compare the bids. Foulds, *supra* note 105, at 528–29.

107. Ross et al., *supra* note 103, at 17.

108. Foulds, *supra* note 105, at 536–37.

because there is no upfront stapled financing offer from the seller's bank, its inclusion in the financing group holds few of the above-described advantages.

The distinction between the original literally stapled deal and other transactions in which the seller's banker–advisor participates in buy-side financing will prove crucial as fact patterns unfold.

B. Banker Conflicts

This subpart draws out conflicts of interest embedded in the banker service practices just described. We explore the conflicts' negative influences on advisory bank incentives, while for the moment deferring legal evaluation. We divide the conflicts into three categories: (1) conflicts arising from past and projected advisory relationships; (2) conflicts created by the terms of the contract of engagement entered into between the advisory bank and client; and (3) conflicts stemming from the bank's performance of multiple functions in the sale process.

1. Relational Conflicts.—Hypothesize an M&A market in which all relationships between targets and advisors and targets and opinion givers are discrete, one-off engagements. The advisor bank parachutes in to work the sale and provides no other services, having no past transactional history with the target or the acquirer; strongly held norms bar it from future dealings with the surviving company. The same goes for the bank opining on fairness, which is separate from the advisor bank. Add a reputational interest on the bank's part in being seen to do an excellent job by third parties, and this hypothetical world yields banks well incented to procure the best deal for the seller and its shareholders.

The hypothetical does not describe the real world of advisory services, which are grounded in relationships rather than discrete engagements.[109] This is only to be expected. For example, the long-term banker–advisor of a selling company has a built-in informational advantage, making it an obvious choice to serve as advisor in a merger. Yet the relationship that creates the advantage can also import conflicts in the form of exterior influences that can negatively affect the judgments and discretionary choices made by banker–advisors and opinion givers. For example, a merger advisor or opinion giver with a preexisting personal relationship with key actors at the seller could cater to their interests.[110] Such catering might privilege the insiders' preferred deal over a more lucrative alternative that makes the shareholders better off. Alternatively, an advising bank

109. *See* Charles D. Ellis, *Attracting Corporate Clients*, *in* INVESTMENT BANKING HANDBOOK 55, 57 (J. Peter Williamson ed., 1988) (stating that CFOs still place considerable importance on established relationships with investment banks).

110. Bebchuk & Kahan, *supra* note 63, at 43.

could act with a view to obtaining or maintaining a lucrative advisory relationship with the managers of the merger's surviving company.[111] Or, in a financial merger, the banker could have a preexisting business relationship with the private equity buyer, along with expectations of participation in future deals. Such influences again threaten to skew the process toward a suboptimal deal pitched to interests other than the selling shareholders'.[112]

The incentive skews having been noted, it also should be noted that the alternative of a discrete advisory engagement does not necessarily eliminate relational conflicts. A seller certainly can jettison a large, full-service advisor with which it has a long relationship and substitute a smaller, more focused boutique bank. But the replacement bank still comes burdened with relational baggage in the form of contacts and past dealings with firms and actors within the industry and in the financing sector. Importantly, the advisor's value stems in part from these very contacts, for the contacts are the sources of the information the advisor brings to the seller's table.

2. Contractually Created Conflicts.—We have seen that on average 80% of the banker–advisor's remuneration is conditioned on successful completion of the deal and pegged to the consideration paid.[113] We also have seen that a second bank brought in only for the purpose of rendering a fairness opinion receives a fixed fee.[114] The contrast is notable: where the opinion giver gets paid even if it renders an unfavorable judgment on the deal, the advisor's payoff lies more in making sure the deal closes than in raising a critical objection to an inadequate price. The performance-based fee gives the advisor an all-or-nothing interest in closing any deal.

To get a sense of the negative possibilities, consider the following hypothetical. Target, Inc. is a company in an industry undergoing consolidation. Its market capitalization is $750 million; a $1 billion sale price would mean a 33 1/3% premium for its shareholders. The company's board of directors feels selling pressure and contacts Unibank to inquire into the desirability of a sale. Under the terms of the engagement, Unibank will receive a flat 0.5% of the purchase price[115] if a sale closes. A $1 billion deal thus nets Unibank $5 million.

As we have seen, Unibank's first job is to the compare the prospective value of an independent Target with the expected yield on a potential

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111. *Id.* at 41–42; Calomiris & Hitscherich, *supra* note 55, at 8.

112. *See* Davidoff, *supra* note 35, at 1587 (stating that ongoing relationships and expectations between a bank and corporate management can influence the bank's decision to find that a transaction is fair in order to protect future business).

113. *See supra* notes 56–59 and accompanying text.

114. *See supra* note 72 and accompanying text.

115. *See* Foulds, *supra* note 105, at 525 (noting that the typical fee for advising on a corporate sale is 0.5% of the transaction's value).

merger.[116] The conflict created by the fee becomes operative immediately; any deal looks better than no deal because the former advice yields the bank nothing and the latter advice yields millions.[117] Let us assume that Unibank advises the Target board that a deal makes sense and conducts a search. Two bidders emerge. Bidder 1 offers \$1 billion in the form of its own common stock. There is a 100% chance that the deal will close. Bidder 2 offers \$1.2 billion in cash, but it will have some problems swinging debt financing. There is only an 80% chance that a deal with Bidder 2 will close. Moreover, if Target enters into serious discussions with Bidder 2, Bidder 1 will walk away.

From the point of view of Target's shareholders, proceeding with Bidder 2 makes sense despite the risk because an 80% chance at \$1.2 billion tied to a 20% chance of being left at the current \$750 million market cap is worth \$1.11 billion, greater than Bidder 1's offer of \$1 billion ([\$1.2 billion × .80 = \$960 million] + [\$750 million × .20 = \$150 million] = \$1.11 billion).[118] Unibank's expectations work differently. Bidder 1 is a \$5 million bird in the hand under the performance fee arrangement. Bidder 2 is worth a lesser \$4.8 million ([\$6 million × .80 = \$4.8 million] + [\$0 × .20 = \$0] = \$4.8 million).

The incentive problem would be ameliorated given a fee based on efforts expended rather than a fee contingent on a deal closing. A variable-contingent percentage fee also could improve things. If Unibank were paid 0.5% up to \$1 billion and 0.075% for any consideration over \$1 billion, pursuit of a risky \$1.2 billion deal with Bidder 2 would be worth \$6 million to Unibank compared to a \$5 million payoff with Bidder 1. But such alternative arrangements are seen only rarely.[119]

Generally, the conflict created by the performance fee skews the advisor bank's incentives in the wrong direction whenever a risky but more valuable alternative crops up, whether in the form of an alternative bidder or a choice over deal terms.[120]

Here again we need to enter a caveat. Advisory fee arrangements have been stable across time.[121] Presumably, the bankers would be just as happy with a different, less conflicted approach, so long as their bottom lines

116. *See supra* text accompanying note 40.

117. We note that the conflict is much ameliorated if Unibank has an existing relationship with Target, for a deal can mean loss of the client to the buyer's investment bank.

118. We are assuming that the sale process is confidential. Given a public announcement, the seller's market capitalization can be expected to be lower than \$750 million if no deal is completed.

119. Variable percentage fees are seen with small companies and private companies. Calomiris & Hitscherich, *supra* note 56, at 6.

120. *See* Foulds, *supra* note 105, at 524 (explaining that a bank may skew an auction in favor of obtaining a higher fee, regardless of whether its actions negatively affect shareholders).

121. *See generally* Bebchuk & Kahan, *supra* note 63, at 38–41 (discussing the most common fee structures for banker–advisors).

remained unaffected. The preference for performance fees accordingly lies with the selling companies, which, once having publicly set a sale process into motion, have a manifest interest in assuring that the deal closes. Failed deals implicate disappointed markets and internal costs manifested in significant stock price declines: Target's market cap falls below the $750 million start point when it announces that its sale process has failed.[122]

3. Conflicts Arising from Multiple Functions.—Conflicts can arise when a financial institution performs multiple functions. Hypothesize a bank engaged to advise *X* Corp. in connection with a projected hostile tender offer for the stock of *T* Corp., an advisory relationship that generates confidential information with manifest value in the trading markets for the shares of both *X* and *T*. The bank has an asset management division and a proprietary trading operation. An informational tip from the bank's merger advisor to its investment advisors and stock traders violates its confidentiality agreement with *X*, not to mention the federal securities laws.[123] Thus do confidential advisory services present an obvious compliance problem when provided by a bank with trading and investment departments. Banks address the problem by constructing internal informational barriers.[124]

We turn now to a more complicated case. A bank sells multiple services, and profit maximization through the sale of service *A* implicates subpar performance of service *B*. To take a famous example, in the post-Enron era regulatory intervention occurred against investment banks charged with having produced in their research departments (service *B*) overly optimistic analyses of companies whose good will they wished to cultivate toward the end of securing underwriting business (service *A*).[125]

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122. A recent study of terminated mergers finds a significantly negative (–4.16%) abnormal return for private targets over a three day event window. *See* Tilan Tang, Bidder Gains in Terminated Deals 10 (June 2014) (unpublished manuscript), *available at* http://ssrn.com/abstract=2503023, *archived at* http://perma.cc/3BG7-PYKC.

123. *Cf.* Tuch, *Investment Banks*, *supra* note 29, at 487 (describing a conflict of interest that arises in the securities trading industry when investment banks draft research reports on public companies they hold or desire to hold as financial advisory clients).

124. *Id.* at 511–12.

125. There resulted the Global Settlement of Conflicts of Interest Between Research and Investment Banking, dated April 28, 2003, between ten large banks and regulators at the Securities and Exchange Commission, the National Association of Security Dealers, the New York State Attorney General, the North American Securities Administrators Association, the New York Stock Exchange, and state securities regulators. Press Release, Fin. Indus. Regulatory Auth., Ten of Nation's Top Investment Firms Settle Enforcement Actions Involving Conflicts of Interest Between Research and Investment Banking (Apr. 28, 2003), http://www.finra.org/Newsroom/NewsReleases/2003/p002909, *archived at* http://perma.cc/9GCU-4V7H. The banks agreed to pay $1.4 billion and reform their conduct of business. *Id.*

With M&A, buy-side lending has emerged as the service *A* that compromises the delivery of sell-side advisory service *B*.[126] A stapled financing package puts the bank on both sides of the negotiating table. In its advisory role it wants a higher price while as a lender to the surviving company it favors a lower price. It simultaneously looks to collect fees in both capacities.

The list of negative possibilities is lengthy. To get a sense of them, return to Target, Inc. and hypothesize that its board of directors is feeling merger pressure but has taken no steps to inquire into sale possibilities. Unibank, a universal bank with both a large lending division and a stable of traditional investment banker–advisors, shows up at Target's door uninvited. Unibank suggests a sale process with its advisory fee at a contingent 0.5%. It also offers to procure financing for up to 90% of the purchase price. Unibank can finance the acquisition either by underwriting bonds or syndicating a loan package (acting as lead lender), collecting fees either way at 1.5% of the loan amount.[127] If Unibank engineers a $1 billion deal and lends 90% of the purchase price, it makes $5 million on its advisory side and $12.15 million on its lending side.[128]

Now assume there are two types of potential acquirers for Target—strategic purchasers and private equity firms. The strategic purchasers are operating companies in the same or related lines of business. They buy using their own stock as consideration or using a mix of own stock and cash. The cash sometimes comes from their own balance sheets and at other times from lenders. The buyout firms, in contrast, finance 90% of the purchase price with borrowed money and have repeat-play relationships with the big banks, including Unibank.

A strategic bidder shows up with a knockout "bear hug" proposal at the start of the process: $1.2 billion in bidder stock for a 60% premium over market but with give ups in the form of negotiation exclusivity and deal protection provisions. This deal nets Unibank $6 million on the advisory

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126. The description in the text does not exhaust the universe of potential conflicts from multiple representations. A bank also could (1) advise two sellers in the same industry; (2) advise both the seller and the buyer; (3) advise two or more buyers of a single company or asset; and (4) provide financing to multiple buyers. *See* David B. Miller et al., *M&A Engagement Letters: Protecting Sellers and Buyers*, STRAFFORD 71 (Nov. 21, 2013), http://media.straffordpub.com/products/m-and-a-engagement-letters-protecting-sellers-and-buyers-2013-11-21/presentation.pdf, *archived at* http://perma.cc/QT2P-C48G.

127. *See* Christine Harper & Julia Werdigier, *'Stapled' Loans Create Potential Conflicts for Merger Advisers*, BLOOMBERG (Oct. 23, 2005, 7:15 PM), http://www.bloomberg.com/apps/news?pid=10000006&sid=aNS.Y5u9qCb8&refer=home, *archived at* http://perma.cc/ETF3-5QVV ("The lead arranger of loans for a leveraged buyout can make 1.3 percent to 1.5 percent of a loan's value . . . .").

128. This was more or less the situation in *In re Rural Metro Corp. Stockholders Litig.*, 88 A.3d 54 (Del. Ch. 2014), where a bank whose financing fees were ten times its advisory fees had a strong incentive to promote its financing role at the expense of its advising. *Id.* at 70.

side and $0 on the loan side. Unibank thus has every incentive to advise Target to resist the squeeze and pursue alternatives that implicate cash consideration financed with loans, particularly with private equity buyers. There is nothing intrinsically wrong with that, but Unibank makes more on the private equity alternative whether or not private equity bidders are likely to make lower offers.

The problem is salient even in the absence of the bear hug offer: whatever the value question on the table, the bank will feel pressure from its corporate loan department to answer in favor of a private equity sale. Moreover, as between two private equity bidders, one of which is open to the staple and the other of which will be finding financing elsewhere, the advisor has a clear preference.

Note that a staple can negatively skew banker incentives even when attaching to all bidders. Let us go back to the staple's original version: the bank's advisory department urges a prospective client to sell all or a part of itself, holding out an assured financing package as a sweetener.[129] The prospective client signs on and the bank conducts an open auction in which all bidders plan to make use of the staple. Although the auction is a win-win for the bank, a perverse incentive creeps in nonetheless. As the bidding goes higher the amount to be loaned under the bank's commitment increases as well; as the principal amount increases the loan becomes riskier and its value to the bank goes down accordingly.

Summing up, a staple aggravates the conflict springing from the performance fee by creating a banker preference for a subset of bidders. It further aggravates the conflict by giving the banker a toehold interest on the opposite side of the negotiating table. And, just as the performance fee builds in a bias towards a conservative posture respecting strategic choices, so does a staple reinforce the conservatism—the easier the buyer's deal terms, in particular the lower the price, the less risky the bank's loan and the more valuable to the bank. But a caveat once again must be entered. As noted above, staples can import advantages to sellers, reducing transaction costs, establishing a price floor, and conceivably importing financing otherwise unavailable.[130]

C. *Summary*

A number of points emerge from this Part's look at investment banker M&A services. First, banker–advisors play a critical role in realizing the best price for target shareholders. To the extent a conflict impairs their service provision, injury is threatened. Second, relational conflicts are inevitable. Third, while some bankers eschew conflicts of interest, many do

129. *See supra* note 101 and accompanying text.
130. *See supra* text accompanying notes 103–107.

not, in some cases seeking them out. Fourth, the bigger the bank the more prone toward conflicts of interest. Fifth, incentive impairments stemming from conflicts are by no means deadweight negatives from the point of view of selling shareholders: some conflicts stem from relationships that generate information of value to selling companies; stapled financing holds out benefits as well as costs. Sixth, bankers and their clients do not use their contracts to minimize conflicts and improve incentives; otherwise the fee would not be performance based.

III. Banker–Client Relationships: Economics and Law

Our review of banker M&A services and industry structure depicts a practice that tolerates banker conflicts, treating them as a piece of a complicated picture of choices and trade-offs. Banks purvey information gleaned relationally, and the source relationships can hold out conflicts. Meanwhile, a sell-side board chooses among a range of vigorously competing banks, some more conflicted than others. A big bank holds out more conflicts but also offers a deeper informational base and a wider range of services including, potentially, financing. Conflicted representation can make cost–benefit sense.

Business people thus see conflicts as problems to be managed. With lawyers, in contrast, conflicts are "red flags" that trigger alarms. When a conflict crops up in a fiduciary relationship, a lawyer's first instinct is to evaluate by reference to "the punctilio of an honor the most sensitive"[131] and counsel avoidance rather than cost–benefit calculation. Corporate law's fiduciary regime protecting the interests of target shareholders triggers a second round of lawyerly concern regarding the conflicts tolerated on the business side.

It looks as if we have set a stage for a classic policy confrontation between economic expediency and fiduciary values embedded in legal mandates. This Part shows that the appearance is deceptive. We begin by examining the banker–client relationship through an economic lens. Unsurprisingly, economic analysis remits the conflicts problem to contractual solution. We then turn to the legal side where the relationship is situated in an agency framework, again unsurprisingly. Bankers, as agents, owe fiduciary duties to their corporate principals, but the law leaves ample room for contractual adjustment accommodating agent conflicts. Now comes the surprise: the accompanying legal process rules synchronize neatly with the features of the relational picture highlighted in the economic analysis.

131. Meinhard v. Salmon, 164 N.E. 545, 546 (N.Y. 1928); *cf.* Tuch, *Investment Banks*, *supra* note 29, at 481 (identifying fiduciary duty as requiring complete and unerring loyalty to another's interests).

A. *The Economics of Banker Conflicts*

Economists define a conflict of interest as a situation in which a party to a transaction can gain by taking actions adversely affecting the counterparty.[132] The definition is capacious, sweeping in actions that lawyers classify as hard bargaining, overreaching, contractual bad faith, and contractual nonperformance, without any need to refer over to fiduciary duty.[133] Where a lawyer inspects the relationship for a duty and proceeds from there, problematizing the conflict if the relationship is fiduciary,[134] an economist views all fact patterns as contractual.[135] Given a conflict, an economist asks how it impacts the parties' incentives and projects their rational, contractual responses.[136]

Here is the basic economic analysis.[137] A rational counterparty, in this case the sell-side board, anticipates the conflict's negative impact and adjusts for it.[138] In the simplest scenario it simply discounts the price until the engagement becomes attractive net of the conflict's costs.[139] The conflicted seller of services will want to forestall discounting and so needs to mitigate the conflict's effect. For an advisory bank, the straightforward way to do this is to build a reputation for adding value to client transactions.[140] Once the bank's future income is staked on the reputation's maintenance,[141] the bank has a strong incentive to make sure that a conflict

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132. Hamid Mehran & René M. Stulz, *The Economics of Conflicts of Interest in Financial Institutions*, 85 J. FIN. ECON. 267, 268 (2007).

133. *Cf. id.* at 268 & n.4 (describing the legal conception of conflict of interest as conditioned on the existence of a fiduciary duty).

134. Tuch, *Investment Banks*, *supra* note 29, at 481–82.

135. *See* Robert Flannigan, *The Economics of Fiduciary Accountability*, 32 DEL. J. CORP. L. 393, 402 (2007) (observing that an economist's primary interest is in analyzing contractual mechanisms that may alleviate agency problems and other opportunism concerns, such as fiduciary breaches).

136. *See* Mehran & Stulz, *supra* note 132, at 278 (demonstrating how financial institutions will consider whether a conflict of interest actually threatens business performance prior to acting on it).

137. More sophisticated formal analyses incorporate factors such as information asymmetries, signaling, banker capability, and market position, showing how banker reputations evolve across time under dynamic conditions. *See, e.g.*, Zhaohui Chen et al., Traders vs. Relationship Managers: Reputational Conflicts in Full-Service Investment Banks 1–2 (Oct. 20, 2013) (unpublished manuscript), *available at* http://papers.ssrn.com/sol3/papers.cfm?abstract_id=2192098, *archived at* http://perma.cc/54Y5-66JN (modeling banker reputations by type of work performed and their use as a governance mechanism to manage conflicts of interest).

138. Mehran & Stulz, *supra* note 132, at 269.

139. *Id.*

140. *Id.* at 277; s*ee also* Jonathan Macey, *The Value of Reputation in Corporate Finance and Investment Banking (and the Related Roles of Regulation and Market Efficiency)*, J. APPLIED CORP. FIN., Fall 2010, at 18, 19 ("[D]eveloping and maintaining a reputation for integrity is costly. At the very least, companies must resist the temptation to pursue opportunities for profit that come *at the expense of their customers*. Encouraging, or even just condoning, the pursuit of such opportunities represents a breach of trust with the customer . . . .").

141. The Board of Governors of the Federal Reserve System defines reputational risk as "the

does not impair its performance.[142] Competition within the advisory sector further sharpens the bank's incentives: a bank giving into conflicts and providing bad service loses market share.[143] Banks thus monitor conflicts, promulgating internal policies and enforcing them with control systems.[144]

Two things follow: first, client injury should not be assumed by virtue of a conflict's existence, and second, even given a negative impact, the conflict may have been taken into account in advance and so would imply no relational breach.[145] Restating these points: conflicts should not be barred by per se rules; indeed, given sophisticated parties, we should presume that conflicts have been recognized *ex ante* and adequately dealt with contractually.

Significantly, this analysis does not predict that the services-seller's interest in minimizing the adverse impact of conflicts reduces their incidence to zero. A bank selling advisory services can be expected to invest in containing its incentive to self-serve only so long as so doing is cost beneficial.[146] And, with investment banking services, minimization of conflicts could be quite expensive since it presupposes that the bank divest all lines of business that create them. Such has not been the case, even as minimalist boutique banks do exist.

To get a better sense of differentiation with the sector, we took the advisors listed in Mergerstat's annual merger advisory top fifty from 1996 to 2013[147] and divided the advisors into four categories: (1) investment bank

potential that negative publicity regarding an institution's business practices, whether true or not, will cause a decline in the customer base, costly litigation, or revenue reductions." Letter from Richard Spillenkothen, Dir., Bd. of Governors of the Fed. Reserve Sys., Div. of Banking Supervision and Regulation, to the Officer in Charge of Supervision at Each Federal Reserve Bank (May 24, 1996), *available at* www.federalreserve.gov/boarddocs/srletters/1996/sr9614.htm, *archived at* http://perma.cc/5BWW-7J8S.

142. Mehran & Stulz, *supra* note 132, at 278.

143. The collapse of Bankers Trust following the disclosure of customer abuse at its swap desk provides a telling example of "the workings of the reputation market." Macey, *supra* note 140, at 27.

144. *See, e.g.*, GOLDMAN SACHS, REPORT OF THE BUSINESS STANDARDS COMMITTEE 17–18 (2011) (describing various groups within the firm that work to resolve conflicts of interest and listing guiding principles underlying the firm's conflict of interest policies), *available at* http://www.goldmansachs.com/who-we-are/business-standards/committee-report/business-standards-committee-report-pdf.pdf, *archived at* http://perma.cc/4NHB-GJTX.

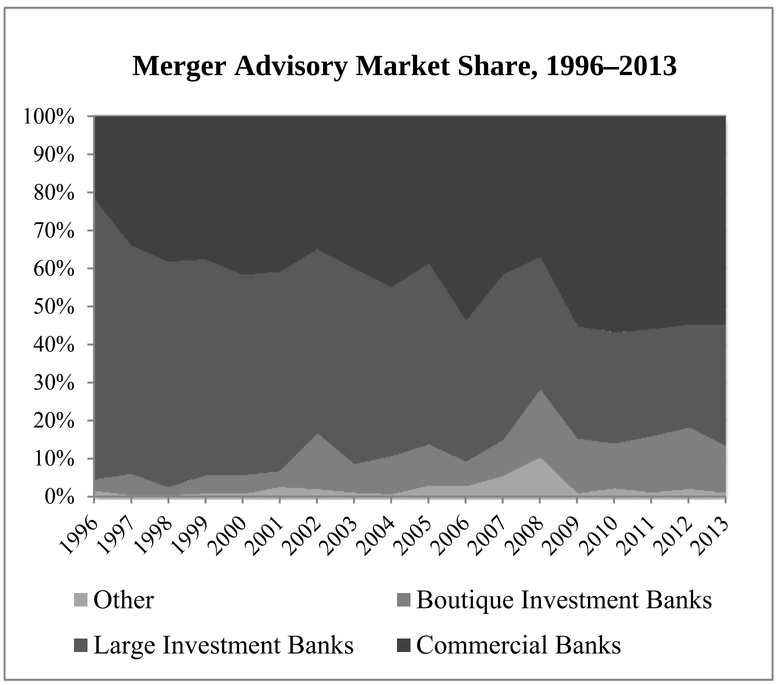
145. *See* Mehran & Stulz, *supra* note 132, at 279 (clarifying that conflicts of interest do not necessarily have adverse impact on services provided by a financial institution if capital markets discount analyst recommendations to adjust for bias).

146. *Id.* at 273.

147. Mergerstat publishes an annual list of the top fifty financial advisors by total deal value. *See* FACTSET MERGERSTAT, 2014 MERGERSTAT REVIEW, at i, x (2014), *available at* http://www.bvresources.com/freedownloads/mergerstatreviewexcerpt2014.pdf, *archived at* http://perma.cc/WY8N-ABPL (stating that Mergerstat has tracked statistics on mergers, acquisitions, and divestitures for over forty-five years, and annually publishes a hardcover report that includes a ranking for financial advisors).

subsidiaries of commercial banks and other large financial companies;[148] (2) large independent investment banks such as Goldman Sachs and Morgan Stanley (irrespective of their categorization as bank holding companies in 2008); (3) boutique investment banks; and (4) advisors not falling into the foregoing three categories (principally private equity and auditing firms). The line between large investment banks and boutique investment banks is drawn by reference to numbers of employees and bankers, underwriting capacity, and the bank's range of activities and breadth of industry coverage.[149] Figure 1 breaks out annual market shares of firms in each category.[150]

Figure 1



148. The "commercial banks" category includes universal banks, institutional lenders, insurance companies, and their subsidiaries. This category does not include investment banks that are only nominally commercial, such as Goldman Sachs & Co.

149. We admit that the line drawing entails judgment calls about quantity and that our approach departs from the practice of financial economists, who divide banks into size categories based solely on market share. *See, e.g.*, Kisgen et al., *supra* note 59, at 188 tbl.2 (using a three-tier ranking system for advisors based on number of acquisitions and market share); P. Raghavendra Rau, *Investment Bank Market Share, Contingent Fee Payments, and Performance of Acquiring Firms*, 56 J. FIN. ECON. 293, 294 (2000) (categorizing banks based on market share).

150. Market shares are calculated based on the total deal volume of the top fifty firms in any given year.

The figure tells a two-part story. On the one hand, large independent investment banks lose market share as large commercial banks acquire them over time. This enhances the potential for conflicts, for commercial bank entry facilitates, inter alia, stapled financing. On the other hand, boutiques steadily gain at the expense of big banks, commercial and independent, taken as a whole.[151] The boutiques' market share increased from 3% in 1996 to 12% in 2013. Boutiques, as monoline shops, are less prone to conflict. They aggressively promote themselves as such.[152]

The Figure also depicts an industry that changes constantly. Boutiques are often founded by bankers who leave big banks to start their own shops.[153] Big banks in turn historically have hired rising stars away from boutiques, maintaining their dominance in the process.[154] That movement was reversed in 2008, when constraints on pay packages made regulated banks vulnerable to poaching by young boutiques holding out bigger bonuses.[155] The back and forth of personnel, taken together with the continued appearance of new boutiques and the volatility of the boutiques' market share, lends the sector a dynamic aspect.

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151. The figures should not be taken to imply that a particular bank, whether in the commercial or large investment bank category, gained or lost market share during the period in question.

152. Scott Bok, CEO of Greenhill & Co., has described the boutique appeal in the following way:

> I think we're kind of a throwback, really. We're a bunch of senior partners who just like advising companies. We don't have any other products to sell you; we don't want to do your financing, we don't want to do your bond underwriting, we don't write research on you, we don't want to sell you foreign currency, we don't want to sell you our wealth management product. All we want to do is give you the best possible advice.

Jonathan Marino, *Rising Sun*, MERGERS & ACQUISITIONS: DEALMAKER'S J., Jan. 2009, at 52, 53; *see also* MORRISON & WILHELM, *supra* note 39, at 303 & n.18 (suggesting that the focused nature of boutique firms immunizes them from conflicts of interest that may affect larger banks, allowing them to give more impartial advice); Joshua Hamerman, *Greenhill's Export: Pure Advice*, INVESTMENT DEALER'S DIG., May 7, 2010, at 1, 18 (quoting Robert Greenhill, boutique advisory firm Greenhill & Co.'s Chairman, who attributes Greenhill's success to its nonconflicted advisory-only model—a feature that separates it from large banks); Joshua Hamerman, *Tech Qonversation*, MERGERS & ACQUISITIONS: DEALMAKER'S J., Aug. 2009, at 44, 44 (quoting Ian MacLeod of investment boutique Qatalyst Partners, who stresses that the Qatalyst model allows advisors "to focus exclusively on providing independent advice to great technology companies"); *Sagent Advisors Formed to Offer Financial Direction, Guidance on Mergers and Acquisitions*, INS. ADVOC., June 21–28, 2004, at 40, 40 (quoting advisor Herald L. Ritch, who remarks that his boutique advisory firm Sagent can offer pure advice, free of trading, investing, or structural conflicts, which meets a "'growing demand'" in America).

153. For example, one of the earliest and best known boutiques, Wasserstein Perella, was founded by two former employees of Credit Suisse First Boston. MORRISON & WILHELM, *supra* note 39, at 302.

154. *See* Stephen J. Morgan, *The Battle of the Bulge Bracket*, WHARTON MAGAZINE, Jan. 1, 2001, http://magazine.whartontest.com/issues/362.php, *archived at* http://perma.cc/GLW7-YEQW (reporting on a large bulge-bracket bank's purchase of a boutique in order to acquire its talent).

155. Christopher Alessi, *Banking on Boutiques*, INSTITUTIONAL INVESTOR, May 2011, at 62, 64.

To summarize, where lawyers look for taints arising from conflicts, counseling prohibition, economic analysis counsels that taints by themselves are not enough to justify prohibitive intervention because the parties already may have adjusted for the underlying conflict in their contract. The economic question is whether a potential for harm survives the contracting process for later realization at the performance stage. The banking sector is well suited to the economic case, for it sees active competition among a range of service providers with conflicts figuring into product differentiation.

B. Legal Treatment: Agency and Contract

We now compare the legal treatment of banker–client relationships.

This might have been a federal law discussion. Banker–advisor firms are broker–dealers within the Securities Exchange Act of 1934[156] and their advisor–employees must register with the Financial Industry Regulatory Authority (FINRA).[157] Numerous FINRA rules apply to investment bankers,[158] but the rules do not touch specifically on advisor conflicts and client duties.[159] State law regimes of contract, agency, and corporation law govern accordingly. The fit with the economic analysis turns out to be surprisingly good.

1. Fiduciary Characterization: Agency and Advisory Functions.— Viewed through a legal lens, banker–client relationships entail the performance of two functions—representation and advice giving. The legal framework differs with the function.

When the banker represents the client at the negotiating table, it acts as an agent: at common law an agency obtains whenever a party acts for another subject to the other's control.[160] A leading Delaware case on banker liability, *In re Shoe-Town*,[161] tersely confirms the characterization: "[The banker] served as an agent of management."[162] Fiduciary duties of loyalty and care follow from the characterization.

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156. *See* Andrew F. Tuch, *The Self-Regulation of Investment Bankers* 16–19 (Wash. Univ. Law Sch. Legal Studies Research Paper Series, Paper No. 14-04-04, 2014), *available at* http://ssrn.com/abstract=2432601, *archived at* http://perma.cc/FD6T-FW9E (arguing that "investment bankers are properly designated as broker-dealers").

157. *Id.* at 16–17.

158. *Id.* at 20.

159. *See id.* at 20–23 (generally describing the subject matter covered by FINRA's rules and explaining that such rules are "piecemeal" and mainly directed at regulating firms, as opposed to individual conduct).

160. RESTATEMENT (THIRD) OF AGENCY § 1.01 & cmt. b (2006).

161. *In re* Shoe-Town, Inc. Stockholders Litig., No. 9483, 1990 WL 13475 (Del. Ch. Feb. 12, 1990).

162. *Id.* at *7.

An agent's duty of loyalty includes a duty not to act as an adverse party to the principal.[163] Conflicts of interest can implicate breaches of duty accordingly. But the prohibition is conditional: the bar lifts if the principal consents to a conflict after full disclosure by the agent.[164] This opening for contracting out from fiduciary responsibility is in turn subject to a proviso: the agent's overall conduct is subject to *ex post* review for good faith and fair dealing.[165] The common law thus withholds from the conflicted agent an assurance of absolute immunity from attack even given consent and disclosure. The practical question is how close the agent can get to immunity.

We turn now to service in an advisory capacity. Here the banker and the client interact one-on-one and the banker does not act for the client in dealing with a third party. Strictly speaking, no agency obtains.[166] This matters, because absent an agency there is no ready-made common law template that comes to bear to impose a fiduciary characterization.

It would seem sensible to extend the fiduciary characterization coupled with the agency to the relationship as a whole, tailoring the duty's particulars for the advisory role. An analogy to legal representation provides a template. Ethical principles applicable to lawyers distinguish between representation and advice giving, termed "counseling."[167] The fiduciary prescription against adverse dealing applies to representation,[168] while the lawyer acting in an advisory capacity is required to "exercise independent professional judgment and render candid advice."[169] Conflicts of interest can impair independence just as they can impair representation and so remain problematic.[170] At the same time, the client remains in the same posture of exposure and reliance that supports imposition of fiduciary duty respecting the agency.

We have found no cases that take up the question whether the fiduciary characterization extends to the banker's actions as an advisor, at least so far as concerns the primary clients—the sell-side corporation and its

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163. RESTATEMENT (THIRD) OF AGENCY § 8.03 (2006).

164. *Id*. § 8.06.

165. *Id.* § 8.06 cmt. d(1). The ethical regime governing lawyers operates similarly. *See infra* text accompanying notes 214–217.

166. *See* RESTATEMENT (THIRD) OF AGENCY § 1.01 cmt. c (2006) (commenting that a service provider who "simply furnishes advice and does not interact with third parties as the representative of the recipient of the advice" is "not acting as an agent").

167. *Compare* MODEL RULES OF PROF'L CONDUCT R. 1.2 (2014) (describing the scope of legal representation), *with id.* R. 2.1 (describing an attorney's advisory role as an aspect of representation).

168. *Id.* R. 1.7.

169. *Id.* R. 2.1.

170. Indeed, we think that the duty to render advice independently is susceptible to a fiduciary characterization, although we are not sure that any outcome determinative consequences would follow therefrom.

board of directors. Such cases as there are concern a secondary issue: whether the selling company's shareholders enjoy the status of fiduciary beneficiaries.

2. Scope: The Status of Shareholders.—Many banker cases turn on the question whether the client's shareholders are direct beneficiaries of its banker's duties. This is unsurprising in view of the prevalence of representative litigation in the wake of merger announcements.

Under Delaware's default rule, bankers owe no duties to shareholders and shareholders accordingly have no direct action against a banker.[171] Significantly, this is not because the banker is classified as a classic arm's-length contract counterparty with the client board. We have already quoted the leading opinion on shareholder duties, *In re Shoe-Town*, for the proposition that the banker is the board's agent.[172] But, in the Delaware court's view, the client board of directors is the only principal in the fact pattern: the banker is not deemed to stand in a relationship of trust with its client's shareholders and thus is not subject to a representative lawsuit for breach of fiduciary duty. We will expand our quotation of *Shoe-Town* to show how this needle is threaded:

> [The banker] served as an agent of management. Its authority was derived by delegation from management. Directors and other governing members of a corporation who are imbued with fiduciary responsibility can be characterized as agents and quasi trustees. It is equally true, however, that those serving as mere agents are generally *not* characterized as trustees and therefore do not stand in a fiduciary relationship with the shareholders. Indeed, it escapes reason to say that an investment bank hired by a management group taking a company private, such as in the present situation, would stand in a relationship with a given corporation and its stockholders similar to the relationship of a trustee to his cestui que trust. In addition, because a fairness opinion or an outside valuation is not an absolute requirement under Delaware law, it makes little sense to strap those investment banks, who are retained, with the duties of a fiduciary.[173]

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171. *See In re* Shoe-Town, Inc. Stockholders Litig., No. 9483, 1990 WL 13475, at *7 (Del. Ch. Feb. 12, 1990) (explaining that bankers serving only as agents are typically not deemed trustees and thus owe no fiduciary duty to shareholders).

172. *See supra* notes 161–62.

173. *Shoe-Town*, 1990 WL 13475, at *7 (citations omitted); *see also* HA2003 Liquidating Trust v. Credit Suisse Sec. (USA) LLC, 517 F.3d 454, 458 (7th Cir. 2008) (refusing to find that a banker–advisor owed a duty to shareholders outside of its contractual duties and noting that "[the plaintiff] wants us to throw out the detailed contract . . . and to make up a set of duties as if this were tort litigation").

Another leading case on banker duties, the New York Appellate Division's opinion in *Schneider v. Lazard Freres & Co.*,[174] goes the other way.[175] Like *Shoe-Town*, *Schneider* is a 1990 decision in a case involving an allegation of banker negligence in connection with the preparation of a fairness opinion. The court used an agency theory to link the shareholders to the banker: the board's special merger negotiating committee was formed to protect the shareholders and engaged the banker toward that end; the committee acted as the shareholders' agent; the banker accordingly acted as the shareholder agent's agent and so stood sufficiently in privity with them to support a direct action.[176]

The two approaches can be distinguished on a theory of the firm grounds.[177] Delaware hews to the traditional model under which the board owes duties to the corporate entity and does not directly serve the

174. 552 N.Y.S.2d 571 (App. Div. 1990).

175. *Id.* at 574–75.

176. *Id.*; *see also* Wells v. Shearson Lehman/Am. Express, Inc., 514 N.Y.S.2d 1, 2 (App. Div. 1987), *rev'd on other grounds*, 526 N.E.2d 8 (N.Y. 1988) (engaging in a similar analysis).

177. Predictably, the Delaware approach has been criticized. The critics would upgrade investment bankers to full fiduciary status with the shareholders as direct beneficiaries. "Gatekeeper" liability would follow along the lines imposed on auditors—applying *ex post* scrutiny for lapses of due care and diligence. *See* Ted J. Fiflis, *Responsibility of Investment Bankers to Shareholders*, 70 WASH. U. L.Q. 497, 513–16, 519–20 (1992) (advocating for such an approach); *cf.* Cameron Cushman, Note, *Liability for Fairness Opinions Under Delaware Law*, 36 J. CORP. L. 635, 649 (2011) (recommending a shareholder cause of action for negligent fairness opinions); Rubenstein, *supra* note 70, at 1724 (same). Contrast those who would prefer to roll back *Smith v. Van Gorkom* and denude the fairness opinion of a central place in the board's demonstration of diligence. *See, e.g.*, Charles M. Elson, *Fairness Opinions: Are They Fair or Should We Care?*, 53 OHIO ST. L.J. 951, 970 (1992) (noting that, because of the variety of valuation approaches used and the influence of interested parties, objective and independent fairness advice is difficult to achieve). Under this line of thinking, valuation opinions should be dismissed completely as intrinsically subjective, *id.* at 970, and useless in most scenarios, *id.* at 1000–03. It follows that a gatekeeper liability regime will never work and the law should not encourage boards to hold out fairness opinions as a basis for shareholder reliance. *See* Carney, *supra* note 82, at 535–36 (rejecting the argument that gatekeeper liability for investment bankers is good public policy). If you need a gatekeeper, free the field of regulatory barriers and let the market for corporate control solve problems through competitive bidding. *See id.* at 538 (suggesting that "[m]arkets may provide the strongest form of protection for minority and public shareholders in takeouts and management buyouts"). But others advocate a more moderate liability-based approach. *See* Dale A. Oesterle, *Fairness Opinions as Magic Pieces of Paper*, 70 WASH. U. L.Q. 541, 557–58 (1992) (recommending that boards of directors should be held liable in shareholders' derivative actions for relying on substandard opinions and that the showing required for proving an aiding and abetting cause of action against an investment banker should be reevaluated).

We reject the analogy to auditors as gatekeepers. Accountants work *ex post* with verifiable numbers. Appraisers of value sometimes do too, but just as often they work with soft future projections. Auditors apply a well articulated body of rules and principles to client accounting treatments and operate under a thick book of best practices. This regulatory encasement provides yardsticks for *ex post* evaluation of auditor performance. There is no comparable body of principles governing the professional activities of bankers, and, failing bankers' formal organization as a profession, none can be expected. The *Shoe-Town* barrier to banker gatekeeper liability makes good sense.

shareholders as an agent.[178] The indirect relationship between the board and the shareholders takes the framework of the common law of trust rather than of agency,[179] with the shareholders emerging as beneficiaries of director trustees rather than as principals. The framing cuts off banker liability—the banker, whatever its tie to the board, certainly has not signed on as anybody's trustee. The New York court, in contrast, is unconcerned about the corporate entity, ignoring it so as to construct a direct agency relationship between the board committee and the shareholders.[180] This facilitates a link over to the banker, who owes the same duties to both principals. The impetus for the treatment lies less in corporate than in tort law.[181]

The *Schneider* approach has not had much traction. In recent cases concerning the characterization and scope of the advisory function, the *Schneider* agency analysis determines no results, to the extent it is mentioned at all.[182] Instead, the cases start where *Shoe-Town* leaves off:

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178. *See Shoe-Town*, 1990 WL 13475, at *6–7 (refusing to find a fiduciary duty between an investment bank hired by a corporation's management and that corporation's shareholders).

179. This follows from the statutory scheme. Consider the basic allocation of power. The relevant Delaware statute provides that the shareholders elect a board of directors in which management power is vested. DEL. CODE ANN. tit. 8, § 141(a)–(b) (2011). If one takes a contextual look at this dispensation against the general legal background, it might appear that the shareholders possess the ordinary rights of owners of property, with the elected directors serving as their agents under a delegation of authority. But such is not the case. In the corporate law model the shareholders do not delegate authority to the board. The board's powers, in the classic expression, are "'original and undelegated,'" springing from the law's provision of the organizational form and its vesting of authority in the board. People *ex rel.* Manice v. Powell, 94 N.E. 634, 637 (N.Y. 1911) (quoting Hoyt v. Thompson's Ex'rs, 19 N.Y. 207, 216 (N.Y. 1859)). Even as the shareholders elect the board, they have no right to tell it what to do. They can only proceed indirectly by removing it or replacing it at the next annual meeting. tit. 8, § 141(k). Agency relationships work differently. Actual authority must be based on the principal's actual manifestation of assent, and the terms of the delegation can be changed at will. RESTATEMENT (THIRD) OF AGENCY §§ 3.01 & cmt. b, 3.06 & cmt. b (2006). Indeed, the delegation can be revoked at will. *Id.* § 3.06 & cmt. c. Neither are the shareholders the legal corporation's owners. They own shares of stock, and, as shareholders, have the rights specified therein or pursuant to corporate law. If one adds up the foregoing incidents of the legal corporation and then looks for an analog in the common law form file, the affinity lies with the trust. Like a trust, the corporate entity takes title to property. *See* RESTATEMENT (THIRD) OF TRUSTS § 40 & cmt. b (2007) ("[I]t is generally stated and usually true that the trustee has legal title . . . ."). Like a trustee, the board of directors has comprehensive power to manage the property and owes fiduciary duties. *See id.* § 70 (stating that a trustee has the power to manage a trust and in acting on this power stands in a fiduciary relationship with the trust's beneficiaries).

180. *Schneider*, 552 N.Y.S.2d at 574–75.

181. The absence of a corporate law duty does not foreclose the possibility of a shareholder suit on the ground that the shareholders are third-party beneficiaries of the advisory contract. *Compare* Baker v. Goldman Sachs & Co., 656 F. Supp. 2d 226, 235–36 (D. Mass. 2009) (finding a controlling shareholder to be an intended beneficiary of an advisory contract), *with* Joyce v. Morgan Stanley & Co., 538 F.3d 797, 802–03 (7th Cir. 2008) (finding that a banker–advisor did not undertake any contractual duties to shareholders).

182. *See, e.g.*, Young v. Goldman Sachs & Co., No. 08CH28542, 2009 WL 247626 (Ill. Cir. Ct. Jan. 13, 2009) (rejecting a *Schneider* claim on the ground that the engagement letter and

there is no presumption, based on agency law or otherwise, that the banker owes fiduciary duties to the shareholders.[183] Rather, it is up to the shareholders to persuade the court that a relation of trust and confidence arose in the circumstances of the particular engagement.[184] It is an uphill fight, given standard-form engagement letters that negate the trust assertion.[185] But shareholder plaintiffs have been known to reach the summit, given the right relational facts.[186]

3. Contracting Out.—Recall that agency law opens a door for contracting out of fiduciary duty: an agent can deal adversely with its principal by procuring advance consent based on full disclosure subject to an overall limitation of good faith and fair dealing.[187] Banker–client engagement letters seek to take full advantage of the opening. This section surveys the result, first taking up disclosure questions and then turning to provisions that limit banker liability and attempt to negate fiduciary status altogether.

a. Disclosure.—The basic requirements of disclosure and consent make eminent sense in the banker–client context. The conflicted banker has an informational advantage. Contracting between the bank and the client respecting the bank's conflict cannot be expected to succeed until the informational asymmetry has been ameliorated. Disclosure evens the field: the client board has choices in the matter (for example, substituting another banker) and needs to make a considered decision regarding the seriousness of the conflict.

Banker–client engagement letters customarily contain boilerplate disclosures of banker conflicts, with the client's execution and delivery of

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fairness opinion made it clear that the banker's duty did not extend to shareholders).

183. *See, e.g.*, *Joyce*, 538 F.3d at 802 (finding that no fiduciary duty existed between a banker–advisor and shareholders stemming from a fairness opinion given by the bank to the company's board of directors).

184. *See Baker*, 656 F. Supp. 2d at 236 & n.5 (applying New York and Massachusetts law, which requires that the plaintiff demonstrate a fiduciary relationship was created based on circumstances beyond the terms of the contract); *Joyce*, 538 F.3d at 802 (applying Illinois law and requiring the shareholders to show special circumstances that give rise to an extra contractual duty); Brooks v. Key Trust Co. Nat'l Ass'n, 809 N.Y.S.2d 270, 272–73 (App. Div. 2006) (requiring allegations that, apart from the terms of the contract, the parties created a relationship of higher trust).

185. *See Joyce*, 538 F.3d at 802 (dismissing a fiduciary claim in reliance on an engagement letter defining the corporation as the client only); CIBC Bank & Trust Co. (Cayman) v. Credit Lyonnais, 704 N.Y.S.2d 574, 575 (App. Div. 2000) (dismissing a fiduciary claim that was contradicted by contractual language). For a case in which the standard restriction to the board of directors blocked a claim related to a fairness opinion, see *Young*, 2009 WL 247626, at *6.

186. *See Baker*, 656 F. Supp. 2d at 236–37 (refusing to dismiss a plaintiff shareholder claim alleging special circumstances where the relationship was "muddy").

187. *See supra* text accompanying notes 164–66.

the letter manifesting consent.[188] But the standard provisions are generic, in effect notifying the client that the bank is a big, multifunctional place that holds out potential conflicts.[189]

Disclosure of conflicts specific to a particular transaction must be tailored with a view to later judicial scrutiny. Delaware has an extensive case law on banker-conflict disclosure occasioned by shareholder litigation over the completeness and accuracy of proxy statements distributed in connection with the merger approval process. Fairness opinions must be described in the proxy statement, and, at the plaintiffs' behest, the Delaware courts conduct searching reviews of disclosures of the opinions' contents.[190]

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188. Here is a sample:

> [Client] acknowledges that [investment bank] is a global, full service securities firm engaged in securities trading and brokerage activities, and providing investment banking, investment management and financial advisory services. In the ordinary course of its trading, brokerage, investment and asset management and financial activities, [investment bank] and its affiliates may hold long or short positions, and may trade or otherwise effect or recommend transactions, for its own account or the accounts of its customers, in debt or equity securities or loans of [client] or any other company that may be involved in the Transaction contemplated by this Engagement Letter. Further, in connection with its merchant banking activities, [investment bank] may have made private investments in [client] or any other company that may be involved in the Transaction contemplated by this Engagement Letter. As a global, full service financial organization, [investment bank] and its affiliates may also provide a broad range of normal course financial products and services to its customers (including, but not limited to investment banking, commercial banking, credit derivative, hedging and foreign exchange products and services), including companies that may be involved in the Transaction contemplated by this Engagement Letter. Furthermore, [client] acknowledges [investment bank] may have fiduciary or other relationships whereby [investment bank] or its affiliates may exercise voting power over securities of various persons, which securities may from time to time include securities of [client] or of potential purchasers or others with interests in respect of the Transaction. [Client] acknowledges that [investment bank] or such affiliates may exercise such powers and otherwise perform its functions in connection with such fiduciary or other relationships without regard to [investment bank's] relationship to [client] hereunder.

Miller et al., *supra* note 126, at 74–75.

189. For an unsuccessful attempt to use a generic disclosure statement to shield a failure to disclose particular facts respecting a conflict, see *In re* Rural Metro Corp., 88 A.3d 54, 105–06 (Del. Ch. 2014).

190. The shareholders must get a fair summary of the work done, including detailed information about key inputs, multiples, discount rates, dates, and the range of values generated. *In re* Cogent, Inc. S'holder Litig., 7 A.3d 487, 511 (Del. Ch. 2010); *In re* Netsmart Techs., Inc. S'holders Litig., 924 A.2d 171, 203–04 (Del. Ch. 2007); *see also* Ehrlich v. Phase Forward Inc., 955 N.E.2d 912, 923 (Mass. App. Ct. 2011) (recognizing the "fair summary" standard). Either a discrepancy between the numbers reported in the proxy statement and those reported to the board, or the failure to report relevant value data supplied to the analyst can result in an injunction against the shareholder vote on the merger. *See, e.g.*, Maric Capital Master Fund, Ltd. v. Plato Learning, Inc., 11 A.3d 1175, 1177–79 (Del. Ch. 2010) (enjoining a vote where the weighted average cost of capital (WACC) used in an opinion had a broader upward range than WACC figures in the boardroom and no disclosure was made regarding internal cash flow projections supplied to the banker). The courts also want the shareholders positioned to understand all factors that might influence the banker's analysis. David P. Simonetti Rollover IRA v. Margolis, No.

An opining banker's conflicts must be disclosed as well. The disclosure requirement is applied against the banker both as regards the board of directors to which the fairness opinion is addressed and as regards the shareholders voting on the merger.[191] Litigation follows over the quality of the proxy statement's disclosures. Scrutiny is strict—failure to disclose and quantify the success contingency in the banker fee arrangement leads to an injunction against the shareholder vote.[192] Any other financial outcomes for the banker following from consummation of the deal also must be disclosed.[193]

3694-VCN, 2008 WL 5048692, at *8 (Del. Ch. June 27, 2008). Class action plaintiffs ask for more disclosure still, including "discussions" of valuation methodologies. Here the courts sensibly balk, asking only for an accurate but literal report. *See In re* 3Com S'holders Litig., No. 5067-CC, 2009 WL 5173804, at *6 (Del. Ch. Dec. 18, 2009) (noting that disclosures do not have to discuss all potential alternatives and recognizing that only accuracy is required); *Netsmart*, 924 A.2d at 204 (same).

191. *See* Blake Rohrbacher & John Mark Zeberkiewicz, *Fair Summary II: An Update on Delaware's Disclosure Regime Regarding Fairness Opinions*, 66 BUS. LAW. 943, 954 (2011) ("Because stockholders need to be aware of a banker's potential conflicts in determining how much weight to place on the fairness opinion, the court has required disclosures in several areas relating to bankers' engagement and their potential interest in the transaction on which they are opining.").

192. *See In re* Atheros Commc'ns, Inc. S'holder Litig., No. 6124-VCN, 2011 WL 864928, at *8–9, *14 (Del. Ch. Mar. 4, 2011) (enjoining the vote, in part, because the specifics of the contingency fee were not disclosed, including the percentage of the fee that was contingent on the success of the deal); La. Mun. Police Emps.' Ret. Sys. v. Crawford, 918 A.2d 1172, 1190–92 (Del. Ch. 2007) (enjoining the vote for failing to disclose the fact that a significant portion of the bankers' fees rested upon initial approval of a particular transaction). *But see* Cnty. of York Emps. Ret. Plan v. Merrill Lynch & Co., No. 4066-VCN, 2008 WL 4824053, at *11 (Del. Ch. Oct. 28, 2008) (finding that the specifics about a contingency need not be disclosed and "that simply stating that an advisor's fees are partially contingent on the consummation of a transaction is appropriate").

193. *See, e.g.*, *David P. Simonetti*, 2008 WL 5048692, at *8–9, *14 (enjoining the vote, in part, for failure to disclose and quantify outcomes relating to warrants and convertible notes from prior transactions).

Strict though the scrutiny may be, critics of the use of contingency fees in fairness-opinion practice remain unsatisfied. They would like to see these conflicts barred. *See* Bebchuk & Kahan, *supra* note 63, at 49–51 (suggesting that fairness opinions written under contingent-fee arrangements should be discounted or a second opinion from a flat-fee banker should be required); Carney, *supra* note 82, at 536–37 (recognizing the existence of proposals to ban success fees). They also note the charge that the opinions are accepted at face value without further scrutiny of their methodologies or assumptions and suggest that opinion practice be revamped so as to afford selling shareholders a stronger, more reliable basis for voting yes. *E.g.*, Davidoff, *supra* note 35, at 1600–01, 1625. "Fairness" remains undefined under Delaware law, *id.* at 1605, making it hard to subject the opinion to collateral attack. The commentators blame the Delaware courts for settling for less. They suggest that the Delaware courts should get their hands dirty at a technical level: the fairness standard should be articulated explicitly, Bebchuk & Kahan, *supra* note 63, at 46–47, and courts should subject fairness opinions to closer evaluation, checking into the relationship between the banker's assumptions and conclusions and demanding more factual detail, *id.* at 47–48. At the same time, the courts should accord fairness opinions less weight in the balance when evaluating board diligence. *Id.* at 52.

We find the criticism unpersuasive. The softness of valuation opinions follows from the softness of valuation as a discipline. Valuation practice could be regularized and hardened, The disclosure requirement, in short, is not a formality.

b. Liability and Scope Limitations.—Engagement letters contain standard provisions designed to insulate the bank from the duties of care and loyalty. On the care side, the provision limits the bank's liability for actions related to the engagement except in cases of gross negligence or willful misconduct.[194] A parallel provision requires the client to indemnify the bank for liability stemming from the engagement other than any liability resulting from its own willful misconduct, gross negligence,[195] or bad

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provided an authority emerged to articulate and impose best practices. Perhaps, as Professor Davidoff has suggested, bankers should organize as a profession and discipline themselves, articulating their own valuation and conflict of interest standards under the gaze of market regulators. Davidoff, *supra* note 35, at 1615–16 (recommending the formation of a public–private Investment Banking Authority that would promulgate standards for valuation practice and supervise internal procedures, requirements, and conflicts at the banks).

Some self-regulation does exist in the sector: the banks have internal review committees that supervise the rendering of fairness opinions and the committees in turn operate under procedural requirements imposed by the FINRA. *See* FIN. INDUS. REGULATORY AUTH. MANUAL § 5150 (2008), http://finra.complinet.com/en/display/display_main.html?rbid=2403&element_id=6832, *archived at* http://perma.cc/6QBN-9PG4 (establishing rules requiring specific disclosures and procedures addressing conflicts in fairness opinions). *But cf.* Michael B. Rizik, Jr. & Matthew M. Wirgau, *Fairness Opinions: No Longer a Laughing Matter*, 25 T.M. COOLEY L. REV. 233, 261 (2008) (noting that the FINRA rules only apply to certain National Association of Securities Dealers "member[s]"). This is minimal compared with requirements imposed on other advisory financial institutions.

But even if fundamental regulatory change is in order, it is unreasonable to look to Delaware courts to affect it. They are institutionally ill-positioned to do so. The missing function is legislative and administrative rather than adjudicative, and the standard-setting process should be informed by insider expertise.

Nor is there any emergency. The main body of criticism of fairness opinions dates from two decades ago, when shareholders were viewed as hapless consumers who innocently relied on whatever a name-brand banker engaged by an entrenched CEO happened to say. That view has changed. The same climate that prompted the criticisms has prompted heightened scrutiny of boardroom processes and decisions both in Delaware courts and in the outside marketplace. William W. Bratton & Michael L. Wachter, *The Case Against Shareholder Empowerment*, 158 U. PA. L. REV. 653, 677–78 (2010). The board of directors has since evolved as a more robust monitoring institution, populated by increasingly independent directors working together to enhance shareholder value with managers incented by equity compensation plans. *Id.* at 678. Merger volume has reached new records again and again, *id.* at 678–79, and everybody takes a hard look at the deals. Fairness opinions certainly could be more informative. But hapless reliance on them is no longer a piece of the fact pattern, if indeed it ever was.

194. Here is a sample:

> You also agree that no Indemnified Person shall have any liability to you or your affiliates, directors, officers, employees, agents, creditors or stockholders, directly or indirectly, related to or arising out of the agreement or the services performed thereunder, except losses, claims, damages, liabilities and expenses you incur which have been finally judicially determined to have resulted proximately and directly from actions taken or omitted to be taken by such Indemnified Person due to such person's gross negligence or willful misconduct.

Miller et al., *supra* note 126, at 99.

195. *See* Marshall P. Horowitz & Joshua Schneiderman, *Negotiating Investment Banking M&A Engagement Letters: Keeping the Investment Bank Incentivized While Protecting Your*

faith.[196] On the loyalty side, the letter states that services are rendered solely for the use of the client's board of directors[197] and that the bank, as an independent contractor, owes duties arising from the engagement only to the company and to no other person; duties are limited to those expressly created under the engagement and fiduciary duties are disclaimed.[198]

Questions arise respecting these provisions' validity and enforceability The trend lies in favor of the provisions.

The liability limitation language is supported by case law.[199] This is unsurprising, for the language tracks the agency law template for opting

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Interests, LEXOLOGY (Apr. 12, 2012), http://www.lexology.com/library/detail.aspx?g=84675f88e 4c0-492e-8535-954518c0c7f5, *archived at* http://perma.cc/RE8D-RSGD (noting that an investment banker will generally insist on this provision).

196. Here is a sample:

> You are not responsible for any losses, claims, damages, liabilities or expenses to the extent that such loss, claim, damage, liability or expense has been finally judicially determined to have resulted primarily and directly from actions taken or omitted to be taken by such Indemnified Person due to such person's gross negligence, willful misconduct or bad faith . . . .

Miller et al., *supra* note 126, at 93; *see also* Ronald Barusch, *Dealpolitik: Why It's Hard to Successfully Sue Your Banker*, DEAL J., WALL ST. J. (Jan. 25, 2013, 11:22 AM), http://blogs.wsj.com/deals/2013/01/25/dealpolitik-why-its-hard-to-successfully-sue-your-banker/, *archived at* http://perma.cc/V7H6-DLY5 (describing an indemnity clause used by Goldman Sachs that included an exception for bad faith).

197. Here is a sample:

> [Client] acknowledges and agrees that all advice and opinions (written and oral) rendered by [investment bank] are intended solely for the use of the Board of Directors in (and only in) their capacity as such, and may not be used or relied upon by any other person, nor may such advice or opinions be reproduced, summarized, excerpted from or referred to in any public document or given to any other person without the prior written consent of [investment bank].

Miller et al., *supra* note 126, at 16.

198. Here is a sample:

> [Client] acknowledges that it has retained [investment bank] solely to provide the services set forth in this Engagement Letter. In rendering such services, [investment bank] will act as an independent contractor, and [investment bank] owes its duties arising out of this engagement solely to the [client] and to no other person. The [client] acknowledges that nothing in this Engagement Letter is intended to create duties to the [client] beyond those expressly provided for in this Engagement Letter, and [investment bank] and the [client] specifically disclaim the creation of any fiduciary relationship between, or the imposition of any fiduciary duties on, either party.

Miller et al., *supra* note 126, at 18. For an alternative drafting strategy, consider the following clause contained in the engagement letter in a case where the banker had been advising the acquirer in a merger, only later to disengage and represent the target: "[Target] agrees that it will not assert any damage, conflict of interest, or other claim against [the bank], [its] affiliates or such other party arising out of [the bank's] relationship with [the acquirer] on the basis of a conflict of interest or otherwise." Joyce v. Morgan Stanley & Co., 538 F.3d 797, 802 (7th Cir. 2008). The drafter makes no attempt to deny the existence of a duty of loyalty or to contract out from under it. It simply gets the beneficiary to waive any claim arising therefrom.

199. *See, e.g.*, HA2003 Liquidating Trust v. Credit Suisse Sec. (USA) LLC., 517 F.3d 454, 457–59 (7th Cir. 2008) (validating liability limitation language in an engagement letter by refusing to find liability on the part of a bank because its lack of prescience did not constitute

out, including the same exclusion of bad faith conduct.[200] A question does arise concerning the more particular meaning of the good faith concept in the banker–client context. The contractual concept of good faith[201] can be expansive or narrow, implying substantive fairness norms where the relationship entails vulnerability and dependence but limiting the parties to rights expressly set out in the contract given arm's-length dealing among sophisticated parties.[202] There also is a parallel, culpability-based good faith concept developed by the Delaware courts in cases where a corporate charter opts out of the duty of care.[203] Choice of law issues could arise as between the two concepts.[204]

How the variant notions of good faith might synchronize in the banker–client context is anybody's guess, for there are no cases. Our sense is that the culpability-based good faith notion would come to bear as a universal backstop, with courts avoiding resort to either expansive or narrow contract law concepts. This approach neatly echoes the engagement letters' exception for acts of "gross negligence, willful misconduct or bad faith."[205]

We now turn to scope limitations and fiduciary disclaimers. Scope limitations that exclude shareholders from beneficiary status are uncontroversial.[206] They take a cue from *Shoe-Town* and confirm that the particular banker–client relationship occupies the default position regarding shareholders.[207]

"gross negligence").

200. *Compare* Miller et al., *supra* note 126, at 93 (providing a bad faith exclusion), *with* RESTATEMENT (THIRD) OF AGENCY § 8.06 (2006) (setting forth a good faith standard).

201. *See, e.g.*, Kirke La Shelle Co. v. Paul Armstrong Co., 188 N.E. 163, 167 (N.Y. 1933) (observing that there is an implied covenant of good faith and fair dealing in every contract).

202. The leading case is *Broad v. Rockwell Int'l Corp.*, 642 F.2d 929, 957 (5th Cir. Apr. 1981) (en banc).

203. *See In re* Walt Disney Co. Derivative Litig., 906 A.2d 27, 47 n.37, 66–67 (Del. 2006) (defining bad faith as an "intentional dereliction of duty, a conscious disregard for one's responsibilities," falling between "(1) conduct motivated by subjective bad intent and (2) conduct resulting from gross negligence").

204. In a Delaware litigation, the issue could arise under the law of another state, with New York as a likely candidate, depending on the engagement letter's choice of law clause. *See* Louis R. Dienes & Alison M. Pear, *An Annotated Form of Investment Banking Engagement Letter*, 25 CAL. BUS. L. PRAC. 107, 120 (2010) (providing a model engagement letter prepared by California lawyers with an alternative of California or New York law). By hypothesis, since the engagement contract creates the agency, the agency law applied to the engagement should be the law chosen by the contract. But the matter is not free from doubt. *See* Shandler v. DLJ Merch. Banking, Inc., No. 4797-VCS, 2010 WL 2929654, at *19 (Del. Ch. July 26, 2010) (refusing to apply the Ohio choice of law provision in an engagement letter to a claim alleging that a bank aided and abetted the selling board's breach of fiduciary duty on the theory that Delaware has the stronger interest in the matter).

205. *See supra* note 196.

206. *See supra* notes 184–186 and accompanying text.

207. *See* Joyce v. Morgan Stanley & Co., 538 F.3d 797, 802 (7th Cir. 2008) (noting that, absent special circumstances giving rise to an extra-contractual fiduciary duty, investment bank

Across-the-board provisions that disclaim a fiduciary duty to the client corporation and its board of directors present more of a problem, for they raise a theoretical question as to whether or not the common law of agency imports a mandatory fiduciary duty. Corporate law precedents suggest that such disclaimers are ineffective.[208] Contrariwise, a disclaimer of fiduciary duty has been given effect in a banker–client case decided abroad.[209] Meanwhile, the limitations and disclaimers in engagement letters follow the pattern for opting out that now prevails in documentation governing limited partnerships (LPs) and limited liability companies (LLCs).[210] But the comparison to LPs and LLPs also sounds a note of caution. LP and LLC disclaimers have explicit statutory backing,[211] statutes in turn prompted by judicial expressions of doubt concerning the limits of the opting-out envelope.[212] In any event, the LP and LLC opt-out envelope remains subject to a contractual good faith limitation.[213]

Engagement letters, in sum, get the bankers comfortably close to immunity respecting conflicts—given disclosure and consent and subject to

owed no such duty to shareholders); Brooks v. Key Trust Co. Nat'l Ass'n, 809 N.Y.S.2d 270, 272–73 (N.Y. App. Div. 2006) (requiring investor to allege that the parties created a relationship of higher trust than would arise from their contracts alone to sustain a cause of action to lie for breach of a fiduciary duty independent of contractual duties). *But see* Baker v. Goldman Sachs & Co., 656 F. Supp. 2d 226, 236–37 (D. Mass. 2009) (denying motion to dismiss with respect to fiduciary duty claim, because a shareholder made sufficient allegations that special circumstances existed to create an extra-contractual fiduciary relationship when an investment bank allegedly knew about and actively solicited plaintiff's faith and trust).

208. *See* Conway v. Icahn & Co., 16 F.3d 504, 508–09 (2d Cir. 1994) (finding that express waivers did not preclude claims for negligence and breach of fiduciary duty against an entity claiming to be a third-party beneficiary to the contract); Neubauer v. Goldfarb, 133 Cal. Rptr. 2d 218, 223–25 (Ct. App. 2003) (holding that a waiver of fiduciary duty to minority shareholders in a close corporation "is against public policy and a contract provision in a buy-sell agreement purporting to effect such a waiver is void"); *see also* Melvin Aron Eisenberg, *The Limits of Cognition and the Limits of Contract*, 47 STAN. L. REV. 211, 250 (1995) ("The core duty-of-loyalty rules governing corporate fiduciaries cannot be waived, but courts may give effect to highly specific agreements that do not present the dangers of systematic unforeseeability and potential for exploitation." (footnote omitted)).

209. *See Australian Sec. and Invs. Comm'n v Citigroup Global Markets Austl. Pty Ltd (No. 4)* [2007] FCR 963 ("[T]he exclusion of the fiduciary relationship was effective, notwithstanding the fact that Citigroup undertook to provide financial advisory services . . . ."). For discussion of this case, see generally Tuch, *Paradox*, *supra* note 29.

210. *See* Mohsen Manesh, *Contractual Freedom Under Delaware Alternative Entity Law: Evidence from Publicly Traded LPs and LLCs*, 37 J. CORP. L. 555, 557, 576–77 (2012) (surveying similar provisions in the operating agreements of LPs and LLCs).

211. *See* DEL. CODE ANN. tit. 6, § 18-1101(c) (2013) (covering LLCs); *id.* § 17-1101(d) (covering LPs).

212. *See* Gotham Partners, L.P. v. Hallwood Realty Partners, L.P., 817 A.2d 160, 167–68 (Del. 2002) (recognizing that the then-current form of § 17.001(d) merely stated that liability could be expanded or restricted by provisions in the partnership agreement but made no mention of the ability to eliminate such liability); Manesh, *supra* note 210, at 561 (noting that the statutes were amended in response to the *Gotham Partners* case).

213. DEL. CODE ANN. tit. 6, §§ 17-1101(d), 18-1101(c) (2013).

exposure for their own willful misconduct, gross negligence, or bad faith. Significantly, the good faith limitation is repeated in every source of law we have traversed—common law, statute, and negotiated contract.

c. Lawyers Compared.—At this point we make reference to the ethical principles governing lawyers as an indirect source of support for our reading of the law of banker–client relationships. One tends to think of lawyer conflicts as prohibited, but the actual rules follow the template of the common law of agency rather closely. As with agency law, the rules start with a prohibition against conflicted representation[214] but then open a loophole—the representation may proceed provided that the lawyer reasonably believes that competent and diligent representation can be provided and the client's informed consent is procured in writing.[215] The loophole's proviso may be restated as a conditional but irreducible prohibition—if the lawyer cannot reasonably believe that competent and diligent representation can be provided, the client's consent is not operative; the conflict is "nonconsentable."[216] Unsurprisingly, the more sophisticated the client the better the case for consentability, with in-house counsel at a large corporation as the archetypical example of a consentable client.[217]

214. DELAWARE LAWYERS' RULES OF PROF'L CONDUCT R. 1.7(a) (2010) ("Except as provided in paragraph (b), a lawyer shall not represent a client if the representation involves a concurrent conflict of interest.").

215. *Id.* R. 1.7(b) ("Notwithstanding the existence of a concurrent conflict of interest under paragraph (a), a lawyer may represent a client if: (1) the lawyer reasonably believes that the lawyer will be able to provide competent and diligent representation to each affected client; . . . and (4) each affected client gives informed consent, confirmed in writing.").

216. *Id.* R. 1.7 cmt. 14 ("[S]ome conflicts are nonconsentable, meaning that the lawyer involved cannot properly ask for such agreement or provide representation on the basis of the client's consent."); *see also* 1 GEOFFREY C. HAZARD, JR. ET AL., THE LAW OF LAWYERING § 11.20 (3rd ed. 2014) (recognizing that similar language under the Model Rules makes certain conflicts nonconsentable). The basic sequence of inquiry in the attorney conflict rules roughly tracks that of corporate law's duty of loyalty—self-dealing transactions between directors and their companies are voidable provided the director discloses fully and gets the consent of the disinterested directors, so long as an unfair transaction still can be voided. In other words: prohibition, followed by permission conditioned on disclosure and consent, followed by a reservation of a core of irreducibly unacceptable situations. The focus of *ex post* review differs, however. With corporate conflicts, the court reviews the decision-making context of the approving board, insisting on consenting independent directors. *See* Benihana of Tokyo, Inc. v. Benihana, Inc., 891 A.2d 150, 173–74 (Del. Ch. 2005), *aff'd*, 906 A.2d 114 (Del. 2006) (requiring an examination of "the interestedness of each of the Voting Directors, as well as the information available to them"). With attorneys the court reviews the attorney's determination to request the client's consent. *See* HAZARD, ET AL., *supra*, § 10.5 ("*[T]he lawyer* must honestly assess the situation and make a reasonable judgment that he or she can still provide competent and diligent representation."). The lawyers' context also holds out some per se rules; for example, representation of both sides in litigation is prohibited without exception. DELAWARE LAWYERS' RULES OF PROF'L CONDUCT R. 1.7(b)(3) (2010); RESTATEMENT (THIRD) OF THE LAW GOVERNING LAWYERS § 122(2)(b) (2000).

217. RESTATEMENT (THIRD) OF THE LAW GOVERNING LAWYERS § 122 cmt. g(iv) (2000) ("Decisions involving clients sophisticated in the use of lawyers, particularly when advised by

Lawyers and bankers thus operate under roughly similar conflicts rules. Yet, in practice, they have very different profiles. Bankers, even as they guard their reputations and monitor client conflicts,[218] take advantage of the law's opt-out envelope and in some cases embrace conflicts.[219] Lawyers who represent large corporations could do the same thing, but in fact do not.[220] They tend to be more risk averse than the bankers,[221] particularly as regards their reputations. They avoid conflicts accordingly, making considerable investments in information flow within their firms to assure that no conflicts occur.[222] The practice of conflict avoidance in turn spawns a set of self-enforcing practitioner norms, norms much more potent in deterring conflicted representation than are the formal rules.[223]

As the economic analysis predicts, what matters here is less the basic legal framework than the actors' particular reputational concerns, concerns that manifest themselves by degree. Even as both bankers and lawyers have a keen interest in protecting their reputations and both invest in conflict avoidance, the respective cost–benefit calculations work differently, with some bankers piling on the conflicts in pursuit of immediate bottom line enhancement. Apparently, in the market for banker services, the conflicts by themselves result in minimal long-term costs in the form of reputational

independent counsel, such as by inside legal counsel, rarely hold that a conflict is non-consentable.").

218. *See supra* note 144 and accompanying text.

219. *See, e.g.*, *In re* Del Monte Foods Co. S'holders Litig., 25 A.3d 813, 826 (Del. Ch. 2011) (concerning a bank involved on the buy and sell side of each stage of the sales process for self-interested reasons).

220. Thomas B. Mason, *Ethics: Conflicts of Interests for Transactional Attorneys*, ZUCKERMAN SPAEDER LLP, http://www.zuckerman.com/media/site_files/165_ABA%20Business%20Law_EthicsConflicts%20of%20Interest%20for%20Transactional%20Attorneys_Mason.pdf, *archived at* http://perma.cc/7TNA-7G2L.

221. *See, e.g.*, C. Evan Stewart, *New York's New Ethics Rules: What You Don't Know Can Hurt You!*, N.Y. BUS. L.J., Fall 2009, at 80, 81 (describing attorneys as risk averse).

222. *See* Susan P. Shapiro, *Bushwhacking the Ethical High Road: Conflict of Interest in the Practice of Law and Real Life*, 28 LAW & SOC. INQUIRY 87, 135–39, 157–59 (2003) (describing the use of electronic databases and screening methods to share information within a firm to avoid potential conflicts).

223. *See id.* at 125–29 (describing five incentives for self-regulation: (1) disqualification from litigation and its related reputational and financial costs; (2) the loss of fees and future relationships through voluntary withdrawal; (3) intrafirm discord arising from conflicts with other attorneys' clients; (4) losing client trust; and (5) expensive or unobtainable malpractice insurance); *see also* W. Terence Jones, *Ethical Issues for Business Lawyers*, *in* ETHICAL LAWYERING IN MASSACHUSETTS § 12.2 (James S. Bolan & Kenneth Lawrence eds., 3rd ed. 2009) (advising that because "the 'fullness' of full disclosure is always a fact question, it is often advisable to decline representation, regardless of the waiver by the clients").

It thus comes as no surprise that there are no cases about merger proxy-statement disclosures concerning conflicted lawyers. *See* Marc I. Steinberg, *Attorney Conflict Scenarios in the M&A Setting*, 33 SEC. REG. L.J. 310, 311 (2005) (describing a "dearth of judicial case law" on ethical M&A practices and responsibilities).

punishment. Meanwhile, the common law of agency throws up no serious obstacles.

C. *Commentary*

We emerge with the economists and lawyers in apparent harmony in their treatment of banker–client relationships. The economists remit conflicts to the contracting parties, and the law facilitates the process, asking only for disclosure as the means to the end. The law accepts this subject to a series of overlapping good faith limitations—the agency duty of loyalty's reservation regarding "good faith and fair dealing," the reservation regarding "gross negligence, willful misconduct or bad faith" in the standard banker engagement letter, and the good faith constraint on statutory opting out.[224] There is a notable harmony of approaches across the disparate sources. There is also a residuum of uncertainty arising from distinctions between the agency and advisory functions and contract and corporate law concepts of good faith. Our sense is that the ambiguities matter little, with the answers to all questions lying in the culpability-based notion of good faith developed in corporate law.

The economists assure us that reputational markets contain any conflict of interest problems left over in the wake of contracting.[225] Our comparative reference to legal practice backs up the assurance, showing us that where a market for services places a high value on undivided loyalty, agents avoid conflicts without any need for legal compulsion.

But the body of cases on which this depiction draws is thin. The Delaware opinions referenced in this Part concern fairness opinions rather than the advisory function. Since no one takes fairness opinions especially seriously,[226] it is easy to conclude that disclosure renders a conflict harmless. The same conflict may loom larger if it impairs the banker's performance of an advisory role with inputs on deal structure and bargaining strategy, raising questions about the adequacy of the disclosure palliative.

The next Part shows the Delaware courts taking a harder look at advisory bank conflicts when the conflicts bear on the question whether a sell-side board has performed its *Revlon* duty to make a reasonable deal. Although the possibility of this connection long has inhered in the structure of Delaware fiduciary law, its recent realization in decided cases alters the calculus of M&A practice and brings banker conflicts to the policy front line for the first time. A theoretical question arises: whether the confrontation implies open conflict between economic analysis and fiduciary norms. We will see in Part IV that the answer is no. *Revlon*

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224. *See supra* notes 165, 194–96, 213 and accompanying text.
225. *See* discussion *supra* subpart III(A).
226. *See supra* note 193.

scrutiny of banker conflicts accepts the contractual zone opened up by the parties, carrying their choice of contract treatment to its logical conclusion.

IV. Hard Looks in Chancery

We have seen that as between fairness opinions and advisory services, the real stakes for all parties in M&A lie in the latter, where the banker's inputs directly impact the transaction's terms. The banker–advisor is there to help the board get the best deal. *Revlon*, in turn, reviews the board's reasonableness in that pursuit. Put the two together and banker conflicts become a problem. The same conflicts that generate minor questions regarding a fairness opinion can create major problems when they compromise the inputs of an actor at the cutting edge of the sale process.

Two recent Delaware Chancery Court decisions, *In re Del Monte Foods Co.*,[227] and *In re El Paso Corp.*,[228] take hard looks at banker conflicts under *Revlon*. A succeeding case, *In re Rural Metro Corp.*,[229] signals that we should expect no letup in the scrutiny's intensity. The upshot is a radical change in the legal posture of banker–client relationships. But, in effecting this change, *Del Monte* and *El Paso* herald no return to old time fiduciary values. They are not motivated by a norm of self-abnegation that runs against the banker, nor do they purport to eliminate contracting out from the banker–client relationship. The *Revlon* overlay has a transformative effect even so, for the question now is whether banker–client contracting inhibits realization of the best deal. The reframing forces the client, the sell-side board, to go into arm's-length mode in dealing with its banker, no longer acting like a passive, consenting beneficiary preserving a valued relationship. The board should be ready to deal with a banker conflict the same way it deals with every other aspect of the merger, with two-fisted bargaining. *Del Monte* and *El Paso*, far from obliterating contract with fiduciary values, *take contract seriously*. If a banker conflict undermines the reviewing court's confidence in the contracting process, the barrier to invalidation by taint that follows from economic analysis falls away.

A. Change of Context: Bankers under Revlon

Conflicted bankers do become embroiled in shareholder litigation over breached fiduciary duties in merger sale processes, despite the *Shoe-Town* barrier and their full use of the opt-out privilege. *Revlon* plaintiffs sue sell-side boards of directors, seeking to establish unreasonable sale processes.[230] Any mishandling of the board's relationship with its banker can figure into

227. *In re* Del Monte Foods Co. S'holders Litig., 25 A.3d 813 (Del. Ch. 2011).

228. *In re* El Paso Corp. S'holder Litig., 41 A.3d 432 (Del. Ch. 2012).

229. *In re* Rural Metro Corp. Stockholders Litig., 88 A.3d 54 (Del. Ch. 2014).

230. *E.g.*, *Del Monte*, 25 A.3d at 817.

such a showing.[231] Importantly, in the *Revlon* context the banker is a piece of the fact pattern, not a defendant. At the same time, however, a banker conflict can be more problematic than in a fairness opinion case like *Shoe-Town*. Fairness opinion cases look only at the banker and the board *inter se*, with the shareholders figuring in only as proxy statement recipients.[232] That limited view makes it easy for a contract and disclosure to deflect attention from the conflicts and their potential impact. *Revlon* shifts the focus to the shareholders as beneficiaries of the board's trustee duty, potentially denuding disclosure and consent of curative power.

Indeed, it can be noted that *Revlon* inquiries into banker conflicts bear a familial relationship to ethical inquiries respecting lawyer conflicts. The lawyer's inquiry has two prongs: (1) the conflict must be fully disclosed to the client, and (2) the disclosing lawyer must reasonably conclude that he or she can still provide competent and diligent representation.[233] The *ex post* decision maker confirms the client's consent and reviews the quality of the disclosure and the reasonableness of the lawyer's determination, weighing the gravity of the conflict.[234] But for one important distinction, *Revlon* scrutiny of banker conflicts is quite similar. As with the lawyers' rules, agency law requires that the conflict must be fully disclosed to the consenting client, here the board.[235] Under *Revlon*, the *client* comes in as a second fiduciary owing a separate duty. Where in legal ethics the fiduciary must reasonably determine that the representation is unimpaired, in a banker case the *client* board of directors must reasonably determine that the conflict does not impair the sale process.[236] The lawyer's term "consentability" is apt. In addition, *Revlon* scrutiny of bankers reverses *Shoe-Town* in part, for under *Revlon* the shareholders get a cause of action.[237] Although the action goes against the board rather than the banker, the relational effect is similar.

At the bottom line, a banker conflict that puts the sell-side board and its deal into *Revlon* jeopardy is effectively prohibited. This destabilizes the

231. *See, e.g.*, *id.* at 818 (finding the board responsible for its banker's actions that led to an unreasonable sale process because the board failed to provide oversight that would have checked their banker's misconduct).

232. *See In re* Shoe-Town, Inc. Stockholders Litig., No. 9483, 1990 WL 13475, at *6–7 (Del. Ch. Feb. 12, 1990) (refusing to find a fiduciary relationship between a fairness-opinion giver and shareholders).

233. *See supra* notes 214–222 and accompanying text.

234. *See supra* note 216.

235. Miller, *supra* note 11, at 10–11 & n.89 (citing RESTATEMENT (THIRD) OF AGENCY § 8.06 (2006)).

236. *See Del Monte*, 25 A.3d at 817 (recognizing the issue as whether the client board breached its fiduciary duty).

237. *Compare* Revlon, Inc. v. MacAndrews & Forbes Holdings, Inc., 506 A.2d 173, 179 (Del. 1986) (holding that a board of directors has a fiduciary duty of care and loyalty to its shareholders when approving a corporate merger), *with In re* Shoe-Town, 1990 WL 13475, at *7 (explaining that bankers serving only as agents owe no fiduciary duty to shareholders).

picture of banker–client relations drawn in Part III without directly altering anything therein. Thus did *Del Monte* and *El Paso* create an appearance of sudden change, for before them there had been only one case in which a banker conflict triggered a *Revlon* violation and then on a fact pattern cluttered with other self-standing violations.[238]

B. An Early Warning

The Chancery Court's hard looks began with a staple. Back in 2005 in a case called *Toys "R" Us*,[239] the Court noted in passing that stapled financing could present a *Revlon* problem.[240]

Toys "R" Us was a straightforward *Revlon* case. The selling board had entered into a merger agreement with a private equity buyer, Kohlberg, Kravis, Roberts (KKR), concluding a long auction process.[241] The plaintiffs made cookie-cutter allegations: the board had failed to pursue alternative strategies to maximize value[242] and had accepted prohibitive deal-protection provisions in the merger agreement.[243] Under *Revlon*, the question was whether the asserted defalcations violated the board's fiduciary duty to pursue the highest reasonable value for the shareholders.[244] The court found the board to have acted reasonably.[245]

Review of the board's reasonableness included a look at the actions of its advisor, Credit Suisse First Boston (First Boston). First Boston passed inspection, but the Chancery Court per (then) Vice-Chancellor Strine, entered a note of disquiet about a staple. First Boston twice asked the board for permission to provide buy-side financing to the bidders, first during the bidding process and second after the signing of the merger agreement—the board denied the first request but granted the second.[246] This displeased the judge:

> That decision was unfortunate, in that it tends to raise eyebrows by creating the appearance of impropriety . . . . Far better . . . if First Boston had never asked for permission, and had taken the position

238. The case was *Mills Acquisition Co. v. Macmillan, Inc.*, 559 A.2d 1261 (Del. 1988). For discussion of this case, see *supra* note 28.

239. *In re* Toys "R" Us, Inc. S'holder Litig., 877 A.2d 975 (Del. Ch. 2005).

240. *See id.* at 1005–06 (acknowledging that stapled financing could create "the appearance of impropriety").

241. *Id.* at 987–95.

242. More particularly, a search for a buyer of a division of the company evolved into a process to sell the entire company. The plaintiffs claimed that instead of expediting that process, the board should have restarted the search. *Id.* at 1001.

243. In particular, the board agreed to a 3.75% termination fee in the merger agreement. *Id.* at 1016. The court ruled that the fee was reasonable on the ground that the winning bid was $1.50 per share higher than the next highest bid. *Id.* at 1017–18.

244. *Id.* at 980, 999.

245. *Id.* at 1007.

246. *Id.* at 1005–06.

> that its credibility as a sell-side advisor was too important in this case, and in general, for it to simultaneously play on the buy-side in a deal when it was the seller's financial advisor. . . . [I]t might have been better, in view of First Boston's refusal to refrain, for the board of the Company to have declined the request . . . .[247]

Nonetheless, the court determined that the financing arrangement did not have a causal effect on the board's sale decision and thus did not justify judicial interference.[248]

The appearance of impropriety stemmed from the staple's effect on First Boston's incentives. Without the staple, the banker stood only on the seller's side of the deal, its fee a function of the sale price and successful closing. As we have seen,[249] the staple put the bank, through its corporate lending department, on the buy side of the deal as well. To the extent the terms of the deal went the buyer's way, the value of First Boston's loan would increase. Fortunately, the staple attached only at a late stage, after the terms had been set.[250] The vice-chancellor also explained that it was not his job to "police the appearances of conflict that, upon close scrutiny, do not have a causal influence on a board's process."[251]

Vice-Chancellor Strine thus left a double gestured signal for the market's interpretation. To express concern about an appearance of impropriety is to talk taint, referencing scrupulous legal practice norms and best practices in venues like government employment rather than the law and practice of bankers and clients.[252] Yet the deal passed inspection. We are reminded of Professor Rock's observation that Delaware courts sermonize without imposing liability as a way of encouraging the development of best practices.[253] The sermon implies a threat that the less-than-best practice that passes inspection today will not be accorded future immunity. But the vice-chancellor also held out comfort when distinguishing between appearances and causal influences, implying that a taint does not imply per se invalidity and that an adverse consequence must be shown.[254]

The Vice-Chancellor's signal was duly noted in the M&A world. Some read it to herald the demise of staples.[255] But, according to Richard

247. *Id.* at 1006.

248. *Id.*

249. *See supra* text accompanying notes 125–28.

250. *Toys "R" Us*, 877 A.2d at 1006.

251. *Id.*

252. The legal profession's actual ethical rules do not make appearances actionable and accommodate conflicts between sophisticated parties. *See supra* notes 214–217 and accompanying text.

253. Edward B. Rock, *Saints and Sinners: How Does Delaware Corporate Law Work?*, 44 UCLA L. REV. 1009, 1016 (1997).

254. *Toys "R" Us*, 877 A.2d at 1006.

255. Hall, *supra* note 100.

Hall of Cravath, Swain & Moore, "cooler heads" prevailed[256] and staples continued to be used freely in their territory of origin auctions of small units of larger companies.[257] Boards of directors in charge of leveraged buyouts of public companies viewed staples with more suspicion.[258] The practice adjusted accordingly and a staple came to mean the added expense of a second banker–advisor, brought in to ameliorate the effects of the conflict.[259] The conservative advice was that avoiding the added expense meant refusing the staple.[260]

Unfortunately, the practice path charted in the wake of *Toys "R" Us* proved unsafe.[261]

C. Del Monte

In *Del Monte*, a more severe banker conflict triggered a *Revlon* violation. In fact, the bank behaved improperly, deceiving its client board and thereby tainting the sale process, but not so noxiously to violate *Revlon* standing alone. There also was an adverse consequence, albeit one in the subtle form of an opportunity cost: the board passively accepted the banker conflict where it should have gone into arm's-length mode and extracted a giveback.

1. The Case.—The banker, Barclays, involved itself on both sell and buy sides at every stage of a lengthy sale process. Del Monte put itself up for sale only after Barclays, with which it had a long advisory relationship, put it into play.[262] Barclays took the first step on its own motion by shopping the company to private equity firms.[263] Indications of interest came in as a result, and the Del Monte board engaged Barclays as its advisor.[264] At that point Barclays disclosed neither its action in stirring up interest nor its intention to provide buy-side debt financing if a deal

256. *Id.*

257. *Id.*

258. *Id.*

259. *Id.*

260. *Id.*

261. Banker conflicts showed up tangentially in three additional cases prior to *Del Monte*. *See* Ortsman v. Green, No. 2670-N, 2007 WL 702475, at *1 (Del. Ch. Feb. 28, 2007) (ordering expedited discovery in a case involving a sell-side banker–advisor participating in buy-side financing); Khanna v. McMinn, No. 20545-NC, 2006 WL 1388744, at *25 (Del. Ch. May 9, 2006) (upholding a complaint that alleged, in part, that a board of directors violated its fiduciary duty by relying on a fairness opinion given by a banker–advisor that had a financial interest in the success of the transaction); *In re* Prime Hospitality, Inc. S'holders Litig., No. 652-N, 2005 WL 1138738, at *1–2, *13 (Del. Ch. May 4, 2005) (rejecting settlement of a *Revlon* claim in a case involving a "clearly conflicted" banker–advisor).

262. *In re* Del Monte Foods Co. S'holders Litig., 25 A.3d 813, 819–20 (Del. Ch. 2011).

263. *Id.* at 820.

264. *Id.*

emerged.[265] Bidding ensued, with each bidder signing a two-year confidentiality agreement that included a "no teaming" provision designed to keep the sale process competitive by prohibiting bidders from sharing information with other bidders or financers.[266] As it happened, Del Monte's board rejected the offers that came in.[267]

Barclays kept at it, encouraging two of the bidders, KKR and Vestar, to team up on a second-round bid.[268] There followed a three-way conversation in violation of the confidentiality agreement,[269] a conversation never disclosed to the Del Monte board. KKR submitted a new, nominally higher bid but said nothing about Vestar's involvement.[270] The board agreed to pursue a deal with KKR and re-engaged Barclays.[271] KKR then asked the board to permit Vestar to join in its bid, and the board, still in the dark about earlier goings-on, consented.[272] Around the same time, Barclays and KKR agreed that Barclays's lending side would provide one-third of the financing for the deal, an arrangement to which the Del Monte board subsequently acceded.[273] The board, seeking to ameliorate the negative inference arising from Barclays's conflict, engaged a second financial advisor.[274]

Del Monte and KKR–Vestar finally came to terms in a merger agreement providing for $19 per share cash and a forty-five day "go shop" period during which Del Monte would be free to entertain higher bids.[275] The Del Monte board, ignoring the fact that Barclays had a buy-side interest in the success of the KKR–Vestar bid, engaged Barclays to administer the go-shop process.[276] Goldman Sachs attempted to horn its way in at that point, offering to take over the go shop.[277] But KKR, after being tipped by Barclays, induced Goldman to back off in exchange for 5% of the financing.[278]

Vice-Chancellor Laster added all of this up to find a *Revlon* violation. He enjoined the shareholder vote for twenty days, which he deemed a length of time sufficient to permit a serious topping bidder to come out of

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265. *Id.*
266. *Id.* at 821.
267. *Id.* at 822.
268. *Id.* at 823.
269. *Id.*
270. *Id.*
271. *Id.* at 824.
272. *Id.* at 825.
273. *Id.* at 825–26.
274. *Id.* at 826.
275. *Id.* at 826–27.
276. *Id.* at 828.
277. *Id.*
278. *Id.*

the woodwork.[279] *Revlon* reasonableness presupposed process integrity and, under *Toys "R" Us*, an investment banker conflict could taint the process so much that even later full disclosure of all the facts would provide no cure;[280] decisions of a deceived board are voidable, and Barclay's had deceived the Del Monte board.[281] In addition, KKR was potentially liable as an aider and abettor of the board's breach, having knowingly broken its confidentiality agreement, concealed its dealings with Vestar, created a conflict in permitting the staple, and skewed the go shop by drawing off Goldman.[282]

If we stop at this point, it looks like the deception by itself undermines the process, triggering the *Revlon* violation. But the Court went further, noting that the problem lay not just in the board's misapprehension of the facts: The facts misapprehended implicated opportunity costs; the board needed sound advice regarding the costs' minimization but never received it because its advisor had disabled itself from so doing in the course of spinning its deception.[283] Barclays crossed the line by failing to come clean when KKR asked for permission to bring in Vestar, silently watching the board accede without advising the board to extract a giveback that increased value to the shareholders.[284] The same failure occurred when Barclays asked for the board's permission to do the staple.[285] Del Monte and KKR–Vestar had not yet agreed on a price at that point; thus did the staple conflict ripen at an earlier, more vulnerable stage of the process than had been the case in *Toys "R" Us*.[286] The board, said the court, should have gotten something in trade for conceding the staple, but instead addressed the problem by engaging another banker at an additional cost to the shareholders of $3 million.[287] The board went on to abdicate its oversight responsibility when it permitted Barclays, by then tainted by the staple, to run the go-shop process.[288]

The merger eventually closed at the agreed $19 per share with the shareholders' approval and despite the injunction.[289] The litigation later was settled for $89.4 million[290]: Barclays contributing $23.7 million and

279. *Id.* at 840.
280. *Id.* at 832–33.
281. *Id.* at 836.
282. *Id.* at 836–37.
283. *Id.* at 836.
284. *Id.* at 833–34.
285. *Id.* at 834–35.
286. *Id.* at 833, 835.
287. *Id.* at 834–35.
288. *Id.* at 835.
289. *KKR Completes Del Monte Deal*, ZACKS INVESTMENT RES. (Mar. 10, 2011), http://www.zacks.com/stock/news/48858/kkr-complets-del-monte-deal, *archived at* http://perma.cc/VN3W-3JLM.
290. Tom Hals, *Del Monte's $89 Million Shareholder Settlement Approved*, REUTERS, Dec. 1,

Del Monte paying $65.7 million.[291] Around $21 million of Del Monte's payment was in lieu of payment to Barclays of its fee.[292] So, roughly speaking, each party contributed fifty-fifty and Barclays walked away from the deal without a fee.[293] Counsel for the plaintiffs picked up $2.75 million.[294]

2. Taking Contract Seriously

a. Relational Characterization.—The key to understanding the *Del Monte* court's analysis lies in distinguishing taint from consequences. The taint was multisided. Barclays worked the deal from three sides, engaging with the buyer and the financiers as well as the selling board, compounding the problem by concealing its relations with the buyer from the board.[295] The *Revlon* violation follows from the court's identification of negative consequences, albeit all of the "might have been" variety. Barclays's concealment of buy-side arrangements disabled the board from negotiating past the buy-team's interest in a low price to get to the upset prices that might have emerged in a competitive bidding. The board then compounded the problem by choosing Barclays to run the go shop over a willing competitor. Barclays had no interest in finding a higher bidder where another bank would have. Finally, the board should have extracted givebacks in exchange for its consent to Barclays's adverse representation.

The court's identification of an opportunity cost in the form of a missed giveback has doctrinal and policy significance. It builds a bridge between the legal framework encasing banker–client relationships and *Revlon* scrutiny on the shareholders' behalf. If the banker, despite a close relationship to the board, plausibly is to be treated in law as a potential arm's-length counterparty privileged to self deal, then in a *Revlon* context focused on short-term shareholder gain, the board–client should be prepared to go into arm's-length mode when the banker asks for concessions, proactively extracting a quo for every quid. The bank is still contracting out under agency law, but now the contracting out process is scrutinized

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2011, *available at* http://www.reuters.com/article/2011/12/01/us-delmonte-kkr-settlement-idUSTRE7B02JZ20111201, *archived at* http://perma.cc/HB7P-9VJD.

291. *Update 2-Del Monte, Barclays to Pay $89.4 Mln in Settlement*, REUTERS, Oct. 6, 2011, http://www.reuters.com/article/2011/10/06/delmonte-barclays-settlement-idUSN1E7951XK20111006, *archived at* http://perma.cc/8WP4-Z4HG.

292. *Id.*

293. *Id.*

294. Divided as follows: $1.6 million for uncovering Barclays "surreptitious activities"; $950,000 for procuring later disclosures to the shareholders regarding the banker's fees, opinions, and relationships; and $200,000 for procuring disclosures about executive compensation tied to the deal. *In re* Del Monte Foods Co. S'holders Litig., No. 6027-VCL, 2011 WL 2535256, at *14 (Del. Ch. June 27, 2011).

295. *Id.* at *5.

under *Revlon*. At the same time, by encouraging the board to deal proactively with the banker, the court shows the M&A world how to make itself safe for future banker conflicts; second bankers at the shareholders' expense will not necessarily do.

A stark takeaway message for selling boards is implied: banker conflicts imply an added layer of responsibility. The selling board must, at a minimum, diligently oversee the banker's work and negotiations on a continuous basis.[296] Restating, since bankers can't be trusted to avoid conflicts and keep their incentives properly aligned, their clients have no business relying on them. If it is arm's length the bankers want, treat them accordingly and protect your own beneficiaries. Such an instruction would not be necessary in traditional fiduciary territory.

Once banker and board find themselves in arm's-length territory, a proactive stance regarding conflict identification makes sense. In the fiduciary context the beneficiary sits back and waits for the fiduciary to disclose the conflict, for only disclosed conflicts are permitted and undisclosed conflicts lead to breaches of duty.[297] At arm's length, one puts the question directly and upfront, getting affirmative representations.

b. Dealing with Deception Under Revlon.*—Del Monte* raises a more particular question for selling boards: what practical steps can be taken to avoid being faulted as a deception victim? Given information asymmetries, deception is always a possibility. The answer once again lies in using contractual devices employed in arm's-length relationships, which can make deception harder and more costly to perpetrate. The board should have required the advisor to represent at the time of engagement that it had not dealt in advance with potential bidders or otherwise violated the terms of its previous engagement—that is, the board should have treated the advisor as a party *without* a duty to disclose. The board could in addition have extracted a promise of continued absolute fidelity to the sell-side interest for the duration of the deal,[298] something that should not be necessary given a fiduciary relationship. The board then actively could have monitored the bankers' performance of the promise. Either a subsequent finding of misrepresentation or a failure to perform the promise of fidelity would result in default under the terms of engagement, and a failure of a condition attached to the duty to pay the fee.

Utmost diligence makes deception less likely without importing an absolute guarantee. It would seem to follow that even a highly diligent,

296. *See In re* Smurfit-Stone Container Corp. S'holder Litig., No. 6164-VCP, 2011 WL 2028076, at *23–24 (Del. Ch. May 20, 2011) (rejecting a *Revlon* challenge because the board "maintained continuous and diligent oversight" of its financial advisor).

297. *See supra* section III(B)(1).

298. The representation of no violations of the terms of the existing contract should also be procured from a bidder subject to a confidentiality agreement.

disinterested board can walk into a deal that violates *Revlon*. The result seems surprising, for *Revlon* is seen as a rule of heightened diligence.[299] But the result is wrought into the inquiry's structure, which demands a process reasonably calculated to result in best price.[300] A deal founded on deception regarding material facts cannot be deemed to result from such a process as an objective proposition, however diligent the approving board. Under *Revlon*, diligence is not a key that automatically unlocks the door to a business-judgment safe harbor; process and transactional substance can collapse into one another.[301] Significantly, the diligent sell-side board is not thereby left in an untenable position as regards liability for breach of fiduciary duty. As to personal liability, a safe harbor obtains—the statutory shield for good faith reliance on an agent's inputs.[302] Moreover, the litigation's outcome is as a practical matter determined at the injunction stage.

c. Staples.—We finally turn to buy-side financing. *Toys "R" Us* and *Del Monte* ascribe staples with a taint. The taint does not result in per se invalidity, but it does trigger searching scrutiny. More particularly, the selling board now bears a burden to contain and counteract the adverse consequences on the banker's incentives.[303] Short of refusing the staple, the selling board must justify it, getting a buyer concession in return or otherwise identifying a shareholder benefit flowing therefrom.[304] Diligence and reasonableness combine to mandate bargaining backbone.

Uncertainty will persist even with a giveback. Assume a concession in the form of a more liberal go-shop term including a right to solicit higher bids. It still will be hard for the board to see its way 100% clear of the taint: what is the value of a larger go-shop envelope when your advisor has zero interest in scaring up a higher bid? To dispel doubts, the board probably must resort to the expedient of engaging a second advisor and putting it in the driver's seat. Once the second advisor displaces the conflicted advisor

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299. *See In re* Toys "R" Us, Inc. S'holder Litig., 877 A.2d 975, 1006 (Del. Ch. 2005) (holding that under *Revlon*, "once directors decide to sell the corporation, they should do what any fiduciary (such as a trustee) should do when selling an asset: maximize the sales price for the benefit of those to whom their allegiance is pledged"); *cf.* Omnicare, Inc. v. NCS Healthcare, Inc., 818 A.2d 914, 929 (Del. 2003) (describing the *Revlon* standard as "enhanced judicial scrutiny").

300. Lyondell Chem. Co. v. Ryan, 970 A.2d 235, 239 (Del. 2009).

301. We commend Professor Miller's nuanced discussion of the doctrinal strands that combine to produce this result. Miller, *supra* note 11, at 8–9.

302. DEL. CODE ANN. tit. 8, § 141(e) (2011).

303. *In re* Del Monte Foods Co. S'holders Litig., 25 A.3d 813, 833 (Del. Ch. 2011).

304. For a case in which the court sustains such a justification, see *In re* Morton's Rest. Grp., Inc. S'holders Litig., 74 A.3d 656, 673 (Del. Ch. 2013). The banker emerged as a potential lender after the bidder reported difficulties in procuring financing. *Id.* The selling board permitted its banker to proceed as lender on the condition that it recused itself from further negotiations, reduced its fee, and still opined on fairness. *Id.* The reduced fee funded engagement of a second banker. *Id.*

from the deal's front line the taint arguably is removed. Significantly, as negative consequences stemming from the sell-side board's allowance of the staple pile up, just saying no at the get-go begins to look like the preferred alternative.

D. El Paso

El Paso turns up the heat several notches. Here the board and the banker made the moves indicated in the conflict-management playbook—the conflict was fully disclosed and the board displaced the compromised banker at the front end of the deal. The court's negative findings cast doubt on the efficacy of standard palliatives and ominously imply that taints from banker conflicts can be disabling per se under *Revlon*.

1. The Case.—El Paso Corp. had two lines of business, an oil exploration and production concern and a pipeline; most of its value stemmed from the latter.[305] Its board, advised by Goldman Sachs, decided to enhance value by spinning off the production business, announcing its decision publicly.[306] At that point Kinder Morgan, Inc. approached El Paso with a bear hug: it proposed to buy the whole company for $25.50 per share and threatened a hostile acquisition if El Paso refused to cut a deal.[307] The board sent the El Paso CEO, Doug Foshee, to negotiate with Kinder Morgan.[308] The board also brought in Morgan Stanley to advise it on the Kinder Morgan negotiation.[309] The reason there was a conflict: Goldman owned 19% of Kinder Morgan (a stake worth $4 billion) and had two representatives on its board;[310] it accordingly had a pointed interest in maximizing the value of Kinder Morgan. But Goldman continued to advise the El Paso board on the possible spin-off.[311] Unsurprisingly, Goldman erected an internal information barrier between the bankers working the spin-off and the bankers in charge of its Kinder Morgan investment.[312] It did not, however, disclose that the lead banker remaining on the spin-off owned $340,000 of Kinder Morgan stock.[313]

305. El Paso's consolidated assets were approximately $24 billion, with the exploration and production business contributing approximately $4.7 billion. *In re* El Paso Corp. S'holder Litig., 41 A.3d 432, 437 n.12 (Del. Ch. 2012).

306. *Id.* at 434–35.

307. *Id.* at 435.

308. *Id.* at 436.

309. *Id.*

310. *Id.* at 434.

311. *Id.* at 435–36.

312. *Id.* at 440.

313. *Id.* at 442.

Foshee and Kinder Morgan soon agreed on a price of $27.55.[314] But Kinder Morgan pulled that offer from the table within a week and substituted a lower one.[315] Foshee caved and agreed to $26.87.[316] A merger agreement was signed within a month.[317] It contained, *inter alia*, a no-shop provision, a superior proposal exception set at 50% of El Paso's assets,[318] matching rights for Kinder Morgan, and a $650 million termination fee representing 3.1% of El Paso's equity value.[319] It also required El Paso to assist Kinder Morgan in concluding a preclosing sale of the exploration division.[320] The premium over El Paso's preannouncement stock price was 47.8%.[321] At no point did the board seek competing bidders or look into possibilities for separate sales of the company's two pieces.[322]

The foregoing, taken alone, might not have gotten the El Paso board into *Revlon* trouble, even as it certainly would have occasioned a close look. But there was more. The board let Foshee do the negotiating and set the merger's terms.[323] It was clear to Foshee that Kinder Morgan would be divesting El Paso's exploration division in order to finance the purchase of the pipeline.[324] Foshee, while negotiating the merger, formulated a plan to put together a management buyout (MBO) of the exploration business from Kinder Morgan after the merger's consummation.[325] He put the proposition to the Kinder Morgan CEO as soon as the ink was dry on the merger agreement.[326] At no point, however, did Foshee reveal the plan to his own board.[327] This deception was bad enough, but Foshee also had misdirected his own incentives: the easier the time he gave Kinder Morgan in the negotiation and the more favorable the deal for Kinder Morgan, the better the prospects for a later Foshee-led MBO of the exploration unit. Arguably, El Paso's own CEO was striving to structure the deal for personal benefit.

There also were problems with Goldman. Before being shunted over to the spin-off, it actively encouraged the El Paso board to placate Kinder Morgan in order to avert a public hostile offer.[328] Nor was it irrelevant on

314. *Id.* at 436.
315. *Id.*
316. *Id.*
317. *Id.*
318. That is, El Paso could accept a better deal for the pipeline separately but not a separate deal on the exploration division.
319. *Id.* at 436–37.
320. *Id.* at 436.
321. *Id.* at 435.
322. *Id.* at 437.
323. *Id.* at 438.
324. *Id.* at 443.
325. *Id.*
326. *Id.*
327. *Id.* at 443–44.
328. *Id.* at 440.

the merger front after Morgan Stanley's appearance. The overall outcome depended on a choice between the spin-off and the Kinder Morgan merger. Goldman fed the board its information about the value of the spin-off, all without having disclosed that the banker in charge held Kinder Morgan stock in his personal account.[329] It also successfully insisted on adherence to the terms of its original engagement, so that it had an exclusive right to advise the board on the spin-off's value, thereby foreclosing the possibility of second-guessing on the spin-off by Morgan Stanley.[330] There was also a spat about fees. Goldman's engagement gave it $25 million if the board went for the spin-off.[331] But, with the spin-off apparently a receding possibility, it demanded, again successfully, a $20 million fee if the board opted for the merger.[332] Meanwhile, Morgan Stanley, at Goldman's insistence, got $35 million if the merger closed but nothing if the board rejected the merger and went for the spin-off.[333] Add this up and Goldman's incentive to push hard for the spin-off was deeply compromised while Morgan Stanley, having been shut out of the spin-off, had every reason to persuade the board to resolve doubts in the merger's favor.

The court ruled that the plaintiffs had a reasonable probability of success on a claim against the board.[334] But the plaintiffs asked the court for an aggressive injunction that avoided the deal protection provisions and allowed El Paso to shop itself further while simultaneously binding Kinder Morgan to complete the merger if no topping bid emerged.[335] That, said the court, was not the deal Kinder Morgan had made.[336] The injunction was refused accordingly.[337]

The merger eventually closed at the agreed price.[338] An unofficial tally indicated that 70% of the El Paso shareholders voted, of whom 98.5% approved.[339] Kinder Morgan and Goldman later settled the litigation. Kinder Morgan paid a $110 million settlement and Goldman waived its fee.[340] Counsel for the plaintiffs walked away with $26 million.[341]

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329. *Id.* at 441–42.

330. *Id.* at 442.

331. *Id.*

332. *Id.* at 442–43.

333. *Id.* at 442.

334. *Id.* at 444.

335. *Id.* at 449.

336. *Id.* at 449–50.

337. *Id.* at 452.

338. *El Paso (EP) Stockholders Approve Kinder Morgan (KMI) Merger*, ISTOCKANALYST (Mar. 9, 2012, 12:41 PM), http://www.istockanalyst.com/finance/story/5719134/el-paso-ep-stockholders-approve-kinder-morgan-kmi-merger, *archived at* http://perma.cc/57V3-7N4P.

339. Matt Levine, *Shareholders Seem Unfazed by Evildoing in Kinder Morgan–El Paso Deal*, DEALBREAKER (Mar. 5, 2012, 1:49 PM), http://dealbreaker.com/2012/03/shareholders-seem-unfazed-by-evildoing-in-kinder-morgan-el-paso-deal/, *archived at* http://perma.cc/3SX8-99S5.

340. Jef Feeley, *Kinder Morgan's $110 Million El Paso Settlement Approved*, BLOOMBERG

2. Taints and Consequences.—El Paso's result rests on two conflicts: Foshee's as well as Goldman's. Foshee's conflict, taken alone, might or might not have triggered a raised eyebrow without a *Revlon* violation following.[342] Similarly, the Goldman conflict, taken in isolation and absent Foshee's deception, might not have sufficed to tip the *Revlon* scale against the merger. Alternatively, had the board reined in Foshee and taken control of the negotiation process, maybe none of the conflicts would have mattered. There are no answers, given the fact sensitivity of *Revlon* cases.

That said, *El Paso* leaves open questions concerning the banker's conflict, its gravity, and its stand-alone impact. The Goldman taint was clear enough, but what were the negative consequences? Absent consequences, *El Paso* can be read to invalidate the merger based solely on the existence of the conflict, arguably a radical departure in the direction of per se prohibition. The opinion coaxes out the conflict's persistence after the engagement of the second banker and then takes care to highlight negative implications. The facts can be read more benignly. Goldman was shunted to one side at an early stage. It did recommend that El Paso come to the table to deal with Kinder Morgan, but Morgan Stanley replicated that advice. Nobody needed to pay Goldman the slightest attention when it officiously raised its voice about Morgan Stanley's fee, which at all events came in the usual form. The valuation numbers Goldman produced regarding the spin-off were indeed suspect, but they hit the table at a stage at which nobody appears to have been suggesting that the spin-off was a viable alternative.

But nothing compels a benign reading. Indeed, as compared to the other conflicts of interest described in this Article, those of Goldman in *El Paso* were the most serious. We have seen banker incentives to get the best deal impaired for a variety of reasons—the banker might be cultivating future business with the target's own managers, the acquiring company, or the bank financing the deal, or the banker might be promoting a substandard deal in order to assure a success fee or a loan origination fee. The stakes in *El Paso* were larger and more immediate because Goldman *owned* a chunk of the acquirer.

Let us consult the dollar figures. Goldman's 19.1% of Kinder Morgan was worth $3,625,474,851 the day before the public announcement of the merger.[343] Goldman's stakes in the merger negotiation stood at

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(Dec. 4, 2012, 12:07 AM), http://www.bloomberg.com/news/2012-12-03/kinder-morgan-s-110-million-el-paso-settlement-approved.html, *archived at* http://perma.cc/7PSW-NJ9P.

341. *Id.*

342. We put off to one side the question whether Foshee breached his own duty to El Paso.

343. According to Kinder Morgan's 2012 proxy statement, Goldman owns 134,826,138 shares. Kinder Morgan, Inc., Proxy Statement Pursuant to Section 14(a) of the Securities Exchange Act of 1934 (Schedule 14A) (March 30, 2012). The stock closed at $26.89 on October 14, 2011. *Kinder Morgan, Inc. Historical Stock Prices*, YAHOO! FIN., http://finance.yahoo

$147,193,376 per dollar paid in or out in greater or lesser consideration paid for El Paso.[344] Of course, a dollar in or out tells one only so much, for profit is not safely assumed for merger acquirers—many mergers are priced so generously for the seller as to result in a loss or a wash for the acquirer.[345] But that result seems unlikely here, and not only because Goldman held two Kinder Morgan board seats and was highly incented to choke off any overpriced deal. The stock market liked the merger. Kinder Morgan stock rose from $26.89 at the preannouncement close to $28.19 on the next trading day, an announcement day gain for Goldman of $175,273,979.[346] The stock hit $30.11 a week and a half later and went on to a peak of $39.85 in April 2012 before settling back down to $32.42 by the time the merger closed on May 25, 2012.[347] Plainly, Goldman's buy-side interest in a $200 million-plus gain on its $4 billion investment in Kinder Morgan dwarfed the $25 million held out by its advisory engagement with El Paso, a figure that arguably should be reduced to $5 million due to the $20 million paid to Goldman in the event the merger closed. This was enough money to turn the head of any member of the firm, an incentive skew impervious to the presence of internal barriers blocking day-to-day information regarding transactional progress.

A "might have been" consequence follows. The El Paso board faced a choice between sale and spin-off, with Goldman working the spin-off. How could any Goldman banker reasonably be expected to offer uninfluenced advice? Once Kinder Morgan showed up, *any* input from Goldman on any aspect of El Paso's strategic choices was highly suspect. It follows that the fact that the Goldman banker left on the deal, as a Kinder Morgan stockholder, stood to gain or lose $13,656 for every dollar more or less paid by Kinder Morgan for El Paso,[348] is not the critical fact. While this is real money for many, it could not be expected to turn the head of a Goldman

.com/q/hp?s=KMI&a=09&b=15&c=2011&d=09&e=17&f=2011&g=d, *archived at* http://perma.cc/4GYD-T3Y7.

344. Per Professor Miller's figures, Miller, *supra* note 11, at 15, El Paso had 771,852,913 shares outstanding and Kinder Morgan had 707,001,570. The cost factor is thus 1.0917273 per Kinder Morgan share, multiplied by 134,826,138 shares held by Goldman.

345. *See infra* notes 429–432 and accompanying text.

346. According to Yahoo! Finance, Kinder Morgan common shares closed at $26.89 on October 14, 2011 and $28.19 on October 17, 2011—the next, post-announcement trading day. Since Goldman owned 134,826,138 shares of Kinder Morgan, this $1.30 post-announcement rise in stock price resulted in a $175,273,979 gain for Goldman. *See supra* note 342.

347. *Kinder Morgan, Inc. Historical Stock Prices*, NASDAQ, http://www.nasdaq.com/symbol/kmi/historical, *archived at* http://perma.cc/KG6Q-HZ68 (selecting "4 years" from the "Select Timeframe" dropdown menu; then see stock prices for October 25, 2011, April 5, 2012, and May 25, 2012, respectively).

348. Miller, *supra* note 11, at 15 ("[E]ach additional $0.25 that Kinder Morgan paid per El Paso share cost . . . [the banker] about $3,414, or . . . for each $0.25 per El Paso share that . . . [the banker] might . . . depress the deal price, he would personally profit by about $3,414.").

banker. Contrariwise, a $200 million-plus gain for the firm certainly would have mattered. Forceful advocacy of a spin-off would have amounted to disloyalty to the banker's employer.

Ideally, Goldman should have been shut out entirely. Had Goldman seen itself as a fiduciary to El Paso, that result presumably would have followed: a conscientious fiduciary can be expected to withdraw voluntarily and immediately when put in this position.[349] Chancellor Strine, in short, was not exaggerating.

So which is it, taint or consequence? The answer depends on one's reading of the facts. If the spin-off was history—a dead-end valuation exercise conducted for compliance purposes—then the Goldman taint triggers the *Revlon* violation on a stand-alone basis (or, at least when taken in tandem with Foshee's deception). On this reading, *El Paso* starts to look like best practices rule making: appearances of conflict by themselves can be disabling. If the spin-off analysis is seen as central to the sale process, then a serious question arises regarding Goldman's incentives: had an un-conflicted banker been working the spin-off maybe it would have emerged as the more attractive outcome, killing the merger. While a "might have been," this is enough to count as a consequence. And the conflict was very severe: had the El Paso board been completely asleep at the switch and permitted Goldman to continue as sole merger advisor, an open and shut *Revlon* violation would have followed without a showing of particular negative consequences. We doubt that anyone would disagree with that.

On balance, *El Paso* does not embrace a rule of per se invalidation. It instead stands for the proposition that consequences can be counterfactual, sensitive to the gravity of the conflict, and tied to the reviewing court's confidence in the overall sale process. When the court concludes that the banker's incentives undermined the contracting process, it makes an economic judgment with legal consequences. This approach was always implicit in the *Revlon* framework.

3. Still Taking Contract Seriously.—As with *Del Monte*, one takeaway for a conscientious board is that consenting to a conflict means going into arm's-length mode and overseeing proactively, monitoring the advisor's activities and using contract to facilitate oversight and position the board to take appropriate action. *Del Monte* and *El Paso*, read together, teach an additional lesson: multiple conflicts have negative synergies under *Revlon*. *Del Monte* combined a staple with surreptitious bid partnering, arguably in

349. *See* Oldham v. Dendrite Int'l, Inc., No. SOM-C-12017-07, 2007 WL 1453482 (N.J. Super. Ct. Ch. Div. May 1, 2007) (acknowledging that defendant's former counsel had "commendably resigned" due to the potential for a conflict in the merger process). Law firms have been known to resign peremptorily due to investment banker conflicts. *See supra* notes 220–23 and accompanying text.

bad faith on the banker's part.[350] *El Paso* combined a keen but marginalized buy-side conflict with the standard performance fee impairment and then threw in a lead negotiator with a private agenda.[351] What might pass in isolation becomes more and more of a problem as the number of agents with adverse interests multiplies.

El Paso adds a kicker. Consent combined with proactivity is not necessarily enough; extreme steps may be necessary. The El Paso board did keep Goldman off the merger and bring in a second banker.[352] It turned out that it should have done more, whether tailoring Morgan Stanley's fee to the occasion or, better, promptly escorting Goldman out of the building. This can be viewed as a consequence of an application of strong fiduciary norms—the taint proves disabling per se. But we think a contractual characterization is more cogent. When you take contract seriously, there comes a point at which you should stop trusting people, cut off the relationship, and walk away.

E. Aiding and Abetting

Bankers can be brought into *Revlon* cases on a derivative liability basis on the theory that they aided and abetted the board's breach in chief. The theory is doctrinally sound,[353] and also holds as regards an acquiring company.[354] The plaintiff must meet a scienter requirement, proving not only the existence and breach of a fiduciary relationship but the defendant's

350. *See supra* text accompanying notes 262–77.

351. *See supra* text accompanying notes 305–32.

352. *In re* El Paso Corp. S'holder Litig., 41 A.3d 432, 440 (Del. Ch. 2012).

353. The substance, that the defendant aided and abetted negligence, finds support in tort law precedent. *See* Anderson v. Airco, Inc., No. 02C-12-091HDR, 2004 WL 2827887, at *5 (Del. Super. Ct. Nov. 30, 2004) ("[A]iding-abetting liability is elastic enough to admit a common, negligent course of action."); RESTATEMENT (SECOND) OF TORTS § 876 (1979) (establishing liability for a tortious act in concert given (a) a common design; (b) knowledge and substantial assistance; or (c) substantial assistance and a self-standing breach of duty); Nathan Isaac Combs, Note, *Civil Aiding and Abetting Liability*, 58 VAND. L. REV. 241, 258–59 (2005) (analyzing the difference between civil conspiracy and the tort of aiding and abetting). Some courts have found liability for aiding and abetting criminal negligence, but the doctrine is not settled. The operative concept, complicity, is open-ended. *See* MODEL PENAL CODE § 2.06 (1962) (providing for accomplice liability if a person promotes or facilitates an offense by (i) soliciting its commission; (ii) aiding or attempting to aid in its planning or commission; or (iii) failing to perform a legal duty to prevent commission); Daniel G. Moriarty, *Dumb and Dumber: Reckless Encouragement to Reckless Wrongdoers*, 34 S. ILL. U. L.J. 647, 659–62 (2010) (explaining the various ways courts have expanded accomplice liability to extend to reckless and negligent crimes and torts).

354. *See In re* Ness Techs., Inc. S'holders Litig., No. 6569-VCN, 2011 WL 3444573, at *1 (Del. Ch. Aug. 3, 2011) (involving a claim that a board of directors breached its fiduciary duty to shareholders with the aid of the acquiring company); *In re* Smurfit-Stone Container Corp. S'holder Litig., No. 6164-VCP, 2011 WL 2028076, at *24 (Del. Ch. May 20, 2011) (same); *In re* Cogent, Inc. S'holder Litig., 7 A.3d 487, 496 (Del. Ch. 2010); *In re* Dollar Thrifty S'holder Litig., 14 A.3d 573, 594–95 (Del. Ch. 2010) (same); La. Mun. Police Emps.' Ret. Sys. v. Crawford, 918 A.2d 1172, 1184 (Del. Ch. 2007) (same).

knowing participation in the breach.[355] These claims accordingly are thought to be hard to prove.[356] They have been pursued only rarely: prior to 2014, bankers have shown up as *Revlon* defendants in an aiding and abetting capacity in only a handful of reported cases, *Shoe-Town* and *El Paso* among them.[357]

Vice-Chancellor Laster's recent opinion in *In re Rural Metro Corporation*[358] highlights the theory's potential to generate big-ticket liability in the right case. And *Rural Metro* was the right case, with facts contrasting notably with those of *Del Monte* and *El Paso*. Here a banker searching for a buy-side financing score effected a textbook skew of a sale process. The banker, RBC Capital Markets, had its eye on financing opportunities in two deals, both its client Rural Metro's and that of a same-industry player's sale process already underway.[359] RBC figured that pushing Rural Metro's sale at the same time as the competitor's could lead to its inclusion in both financing groups.[360] Unfortunately, it did not disclose the play to the client, even as it eschewed any search for strategic buyers.[361] The strategy promptly blew up when confidentiality agreements in the other deal caused its bidders to refrain from bidding for Rural Metro.[362] Rural Metro's sale process went forward even so, with few bidders participating.[363] A disappointing bid finally was approved by the Rural Metro board.[364] RBC all the while was secretly communicating with the bidder, tipping it to goings-on in the Rural Metro boardroom as RBC tried to secure a place in the financing group.[365] RBC also was adjusting the numbers in its valuation of Rural Metro downward for the purpose of making the low-ball bid look attractive in its fairness opinion.[366] The

355. Allied Capital Corp. v. GC–Sun Holdings, L.P., 910 A.2d 1020, 1039 (Del. Ch. 2006).

356. *See* Binks v. DSL.net, Inc., No. 2823-VCN, 2010 WL 1713629, at *10 (Del. Ch. Apr. 29, 2010) ("The standard for an aiding and abetting claim is a stringent one, one that turns on proof of scienter of the alleged abettor."); *Allied Capital*, 910 A.2d at 1039 ("[T]he test for stating an aiding and abetting claim is a stringent one . . . .").

357. *See In re* Celera Corp. S'holder Litig., No. 6304-VCP., 2012 WL 1020471, at *28 (Del. Ch. Mar. 23, 2012), *aff'd in part, rev'd in part*, 59 A.3d 418 (Del. 2012) (raising an aiding and abetting claim against Credit Suisse); *In re El Paso Corp.*, 41 A.3d at 432, 448 (Goldman Sachs); *In re* Shoe-Town, Inc. Stockholders Litig., No. 9483, 1990 WL 13475, at *7 (Del. Ch. Feb. 12, 1990) (Shearson Lehman).

358. *In re* Rural Metro Corp. S'holders Litig., 88 A.3d 54 (Del. Ch. 2014).

359. *Id.* at 91–92.

360. *Id.* at 91.

361. *Id.*

362. *Id.* at 70.

363. *Id.* at 71.

364. *Id.* at 78–79.

365. *Id.* at 95.

366. *Id.* at 95–96.

successful bidder, licking its lips, never did include RBC in the financing group.[367]

This case, unlike *Del Monte* and *El Paso*, raises no issue as between taint and consequence. On these facts the court did not need to hypothesize "might have been" counterfactual scenarios to show the negative dollars and cents implications for the sale process of the banker's conflict. Nor was scienter on the banker's part a problem, so purposive had been its course of conduct.

The case still got a lot of publicity as a clear-cut demonstration of aiding and abetting's liability potential.[368] The banker, which walked away with only a $5 million fee, now is potentially on the hook for damages based on the value of the company as a whole.[369] The case also highlights a plaintiff-friendly quirk in Delaware law. The directors whose breach was being aided had already settled.[370] They would, had the matter been litigated, have enjoyed the protection of a § 102(b)(7) liability shield[371] so that money damages required a showing not just of an unreasonable sale process but of bad faith. The court, following the logic of existing applications of § 102(b)(7), declined to extend the protection of the board's shield to RBC.[372] The bank was thus liable for damages based on a showing of an unreasonable sale process, a showing that would have been inadequate to support liability against the directors whose breach it aided and abetted.

There is something unsporting about the treatment differential. Indeed, one gets the sense that the shareholder plaintiffs have finally found a way around *Shoe-Town*, nailing the banker directly and emerging as de facto fiduciary beneficiaries of a deep-pocket defendant. The court adds to this sense when it describes the treatment as a species of gatekeeper liability, justified for its deterrent rather than compensatory properties[373]—much like the fraud-on-the-market litigation mill operated by the federal courts under SEC Rule 10b-5.[374]

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367. *Id.* at 78–79.

368. *See* E-mail from Eric Klinger-Wilensky, Morris, Nichols, Arsht & Tunnell LLP, to authors (June 25, 2014) (on file with authors) (explaining that, from a practitioner's perspective, banker engagement letters have evolved in the post-*Rural Metro* world).

369. *Rural Metro*, 88 A.3d at 69, 107–09. RBC may be able to reduce its liability on a contribution theory. *Id.* at 109.

370. *Id.* at 79.

371. DEL. CODE ANN. tit. 8, § 102(b)(7) (2011); *Rural Metro*, 88 A.3d at 85–86.

372. *Rural Metro*, 88 A.3d at 86.

373. *Id.* at 88.

374. *See* William W. Bratton & Michael L. Wachter, *The Political Economy of Fraud on the Market*, 160 U. PA. L. REV. 69, 100–18 (2011) (showing that fraud-on-the-market cannot be justified as a compensatory tort and that its proponents fall back on a deterrent justification, undermining their own case).

These implications, while unfortunate, are only just that. *Rural Metro* holds out no structural change in the law of banker–client relations. The facts are egregious and the derivative liability theory is well-established. The takeaway for sell-side boards is unchanged from *Del Monte* and *El Paso*—the board should treat a conflicted banker at arm's length and monitor closely. The banker–client contracting pattern remains undisturbed, even impliedly. As we have seen, exculpatory provisions exclude bad faith actions,[375] and knowing participation in a breach of a client's fiduciary breach surely falls within anyone's concept of bad faith.

F. *Law, Economics, and Consequences*

Part III's economic analysis of banker–client relationships[376] held out two strong warnings. First, the existence of a conflict that negatively affects incentives does not by itself impair a transaction because the bank, constrained by reputational concerns, does not necessarily act on the conflict. Second, even if the conflict negatively impacts the bank's performance, the possibility may have been priced in *ex ante*. *Del Monte* and *El Paso* traverse neither warning. The first warning amounts to a plea for fact sensitivity and avoidance of per se barriers. *Revlon* inquiry is all about fact sensitivity; it imports no general interdiction against conflicted bankers.[377] Questions can be asked about the gravity of the negative consequences on which the cases rely. But we think counterfactual possibilities should count as consequences, particularly given the preliminary, preclosing process context of *Revlon* litigation. As to the second warning, *ex ante* pricing only solves all problems given complete information. Once the complete information assumption is relaxed, opportunism becomes a distinct possibility, and information asymmetries are wrought into advisory relationships. In any event, there is no evidence of fee discounting in trade for conflicts on the facts of these cases—in fact, that is what Vice-Chancellor Laster was asking for in *Del Monte*.[378]

The only residual economic objection would lie in market disruption: the parties contracted and the court pulverized the contracts. Moreover, a market for reputation shapes banker–client relationships;[379] judicial intervention pretermits the market's operation. Both points are accurate, but unpersuasive when mooted as objections. To make the contracts inviolate is to shut down *Revlon* scrutiny altogether: this is judicial review of a contracting process, justified due to the possibility of skews due to agency

375. *See supra* notes 194–195 and accompanying text.

376. *See supra* text accompanying notes 132–146.

377. *See* Revlon, Inc. v. MacAndrews & Forbes Holdings, Inc., 506 A.2d 173, 185 (Del. 1986) (emphasizing the particular factual circumstances giving rise to director breach of fiduciary duties).

378. *In re* Del Monte Foods Co. S'holders Litig., 25 A.3d 813, 844 (Del. Ch. 2011).

379. *See supra* subsection III(B)(3)(c).

costs. There is no way to cabin off the banker–client contract from the others in the cluster. It also bears noting that in both cases the court intervened with minimal damage to the contract in chief, the merger agreement.[380]

Indeed, the Chancery Court here acts less as a disrupter of the reputation market than as an important participant therein. Conflicted actors suffer negative reputational consequences only to the extent that facts probative of opportunistic conduct become public. Private litigation opens up otherwise black boxes, with the Chancery Court taking the lead role in highlighting hidden facts.

The blowback in the wake of the *Del Monte* and *El Paso* decisions makes sense accordingly. The opinions register as strong negatives in the market for banker reputation, not only as regards their bottom line judgments but as regards facts revealed. And, as we have seen, reputation matters critically in the economics of financial service provision.[381] Protests are only to be expected. One can ascribe the protests' motivation to honor impugned. But we prefer to look to threats to future cash flows.

An interesting question arises as to whether these threats actually flowed through to the banks' bottom lines. Observers have noted that unconflicted boutique banks have been showing up high in the league rankings in recent quarters, attributing market-shifting impact to the Chancery Court.[382] We ran a check on this, drawing on the Thomsen One quarterly top 25 league ranking for U.S. deals, and separating the banks on the list among large commercial banks, large independent banks, and boutiques.[383]

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380. *In re* El Paso Corp. S'holder Litig., 41 A.3d 432, 452 (Del. Ch. 2012) (denying a motion for a preliminary injunction and leaving the merger decision to the shareholders); *Del Monte*, 25 A.3d at 844–45 (enjoining vote on the merger for only twenty days).

381. *See supra* notes 132–44 and accompanying text.

382. *See supra* notes 16–19 and accompanying text.

383. *See supra* text accompanying notes 148–150 and Figure 1.

Figure 2

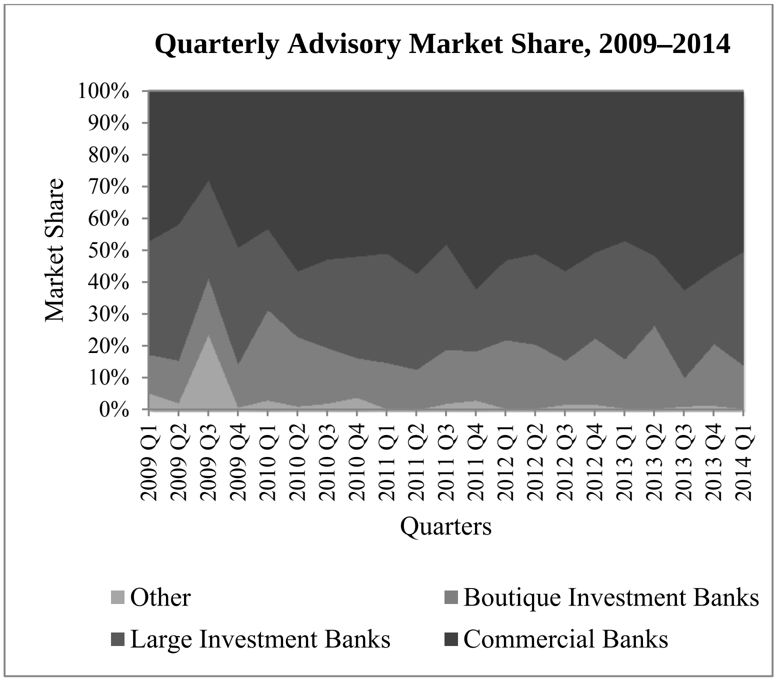

Figure 2 depicts the results. Clearly, the boutique sector has been doing well since *Del Monte* was decided in the first quarter of 2011. No doubt many factors have contributed to this, most importantly secular trends in the merger market and movement of key personnel away from big banks.[384] Seller aversion to conflicts also should be cited—one study offers suggestive evidence of increasing client sensitivity to conflicts going back decades.[385] At the same time, the market share pattern remains volatile, and the recent figures show no clear-cut trend in the boutiques' favor.[386] So

384. Alessi, *supra* note 155,at 64.

385. *See* Agrawal et al., *supra* note 40, at 692–94 (studying mergers in which seller and buyer share a common advisor and showing growing evidence that companies have avoided sharing advisors since the 1990s).

386. The first quarter 2014 numbers in Figure 2 reflect the attribution of boutique status to Paul J. Taubman, a retired Morgan Stanley banker who was the sole advisor in the Comcast acquisition of Time Warner Cable. *See generally* Marcus Baram, *Paul J. Taubman, The Merger King Behind the Massive Comcast-Time Warner Cable Deal*, INT'L BUS. TIMES (Feb. 13, 2014, 1:34 PM), http://www.ibtimes.com/paul-j-taubman-merger-king-behind-massive-comcast-time-warner-cable-deal-1555284, *archived at* http://perma.cc/EX98-75X3 (reporting that Taubman has served as an independent advisor in "some of the biggest deals in recent years" since being pushed out of Morgan Stanley in 2012). Had Taubman been classified as "other," the boutiques' market share trend would be pointing downward. *See Mergers & Acquisitions Review: Financial Advisors, First Quarter 2014*, THOMSON REUTERS 8 (2014), http://dmi.thomsonreuters.com/Content/Files/1Q2014_Global_MandA_Financial_Advisory_Review.pdf, *archived at* http://perma

while it is not unreasonable to put the Chancery Court's reputational inputs on the list of influences, the market share figures provide no basis for attributing *Del Monte* and *El Paso* with game-changing structural impact.

It also has been commented that stapled financing disappeared after *Del Monte*.[387] We checked on this point too. A study of mergers closed between 1998 and 2005 provides a base point, identifying either a seller–advisor staple or past financing relationship in 13% of the deals.[388] To see whether anything has changed, we compared private equity buyouts with a consideration over $100 million that closed in 2006 (at the height of the buyout frenzy), with those that closed in 2012 (the year beginning ten months after the *Del Monte* decision). We found staples for 7% of the 2006 deals and 12.5% of the 2012 deals.[389]

While the raw numbers signal no departure from the past pattern, closer inspection reveals a significant narrowing of usage. Of the twelve staples we identified in 2012, only one involved the sale of a publicly traded company.[390] The rest remained in the territory of the original staple, attached to sales of portfolio companies by private equity firms or of subsidiaries by operating companies. There arises a strong implication of judicial impact: *Revlon* creates a litigation threat only when public companies are bought out and as to these deals staples have almost disappeared.[391]

It seems that actors in M&A continue to find staples advantageous, but only in their original, narrow usage where the justifications are strongest. Outside that territory, significant legal risks now attend their use. So, even as *Del Monte* and *El Paso* have triggered no radical restructuring of the banking sector, they have changed the practice, reducing the salience of conflicts stemming from multiple service provision.

Does this amount to overkill? Significantly, the one public company staple showing up in the class of 2012 was tested in the Delaware Chancery.[392] It passed because the selling board qualified it within the parameters outlined in *Del Monte*: the purchaser really did need financing from its advisor, which withdrew from an advisory role and took a pay cut that funded the engagement of a second bank.[393] To us this amounts to

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.cc/V923-FXW2 (showing that Taubman is individually ranked in eighth place in Thomson Reuters' Top 25 league ranking for U.S. deals for the first quarter of 2014).

387. *See supra* note 18 and accompanying text.

388. Cain & Denis, *supra* note 59, at 15.

389. We used the S&P Capital IQ database. More particularly, in 2006, 12 out of 172 transactions had the seller's advisor in the buyer's finance group; in 2012 it was 13 out of 104.

390. This was the sale of Morton's Restaurant Group, Inc. to Landry's, Inc. *In re* Morton's Rest. Grp., Inc. S'holders Litig., 74 A.3d 656, 660, 673 (Del. Ch. 2013).

391. At the same time, the staple's price-floor function imports more of a benefit when the target is not publicly traded. *See supra* note 104 and accompanying text.

392. *Morton's*, 74 A.3d at 660, 673.

393. *Id.* at 673. We note that the standard of review in *Morton's* was bad faith. *Id.*

ordinary course adjustment rebounding to the selling shareholders' benefit, not overkill. It also contravenes the charges of the critics on the opposite side: these cases are anything but toothless.

V. Regulatory Alternatives: Per Se Prohibition and Safe Harbors

Del Monte and *El Paso* amount to an external shock to actors in the M&A world. The cases trigger reconsideration of standard practices. Solutions must be decided upon under uncertainty. When conservative advice follows, expectations are disrupted. But failure to follow inconvenient conservative advice creates risks. At the same time, the cases leave a lot of observers unsatisfied: some want more in the way of policing from the Chancery, while others think *Revlon* jurisprudence has gotten out of hand.[394]

In this Part we ask whether there might be a better way—a regulatory course imparting greater certainty while simultaneously leaving shareholder interests unimpaired. We experiment with two alternative paths, one stricter and the other more accommodating, both rule based.

The stricter path, charted in subpart A, is per se prohibition of conflicts, posed by analogy to the law governing auditor–client relationships. We start by considering a broad-brush ban. This proves neither feasible nor desirable. We accordingly narrow the scope and consider a prohibition applied only to stapled financing. This proves feasible without being clearly superior to case-by-case review under the open-ended *Revlon* standard.

The more accommodating path, charted in subpart B, narrows the range of *Revlon* exposure by dredging a safe harbor for conflicted banker engagements. We draw on the case law respecting fairness opinions and the practice response to *Toys "R" Us* to propose a two-step qualification for safety: full disclosure by the conflicted banker to the board and the shareholders coupled with engagement of a second, unconflicted banker. In most cases this combination should assure a reasonable sale process, but not in all. The matter accordingly comes down to a trade-off: enhanced relational clarity for selling boards and their bankers versus *Revlon* scrutiny covering the entire range of process impairments. Many would choose the former, particularly in light of the perception of a litigation explosion in the M&A field. We choose the latter, pointing out that the zone of safety would turn out to be surprisingly small. We also find ourselves untroubled by uncertainty in this context. In our view, counsel can handle these problems.

394. *See supra* notes 8–12 and accompanying text.

A. *Per Se Prohibition*

Unlike bankers, auditors are organized as a profession and owe well-articulated duties to their clients.[395] But very much like bankers, profit-seeking auditors have in the past embraced conflicted representation.[396] Eventually, however, Congress and the Securities and Exchange Commission (SEC) intervened to forbid the conflicts, articulating a list of per se prohibitions.[397] This subpart takes a look at the evolution of the auditor rules and considers the possibility of per se prohibition of investment banker conflicts by analogy.

1. Auditor Duties and Prohibition.—Like lawyers, auditors owe specially tailored duties to their clients. Unlike lawyers and more like bankers, they have proved insensitive to their reputations regarding conflicted representation. As a result, they stumbled into a regulatory crisis, emerging under specially tailored conflict prohibitions.

Auditors are held to a standard of care and, unlike bankers, are subject to direct shareholder actions for negligent misrepresentation.[398] They also follow exhaustively articulated professional standards when conducting audits.[399] Among other things, the auditor must remain "independent."[400] Independence in turn derives much of its meaning from a long list of prohibited relationships.[401]

Prior to 2000, the prohibited list did not include most non-audit consulting services.[402] In the 1990s the big accounting firms aggressively took advantage of this, developing large consulting arms that provided

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395. *See generally* William W. Bratton, *Shareholder Value and Auditor Independence*, 53 DUKE L.J. 439 (2003) (arguing for a legal positivist approach to auditors' duties and rejecting the principal–agent paradigm).

396. *See, e.g.*, *id.* at 441–42 (discussing the Enron scandal and the accompanying failure of Enron's auditors).

397. *See* Strengthening the Commission's Requirements Regarding Auditor Independence, 68 Fed. Reg. 6006, 6007 (Feb. 5, 2003) (to be codified at 17 C.F.R. pts. 210, 240, 249, 274) (promulgating regulations following the enactment of the Sarbanes-Oxley Act aimed at reducing auditor conflict).

398. As with bankers under New York law, the theory is that the shareholders are in "near privity" to the contract between the auditor and the corporate entity. *See* Credit Alliance Corp. v. Arthur Andersen & Co., 483 N.E.2d 110, 119 (N.Y. 1985) (requiring "the existence of a relationship between the parties sufficiently approaching privity").

399. The standards are articulated by the Public Company Accounting Oversight Board. REFERENCES IN AUDITORS' REPORT TO THE STANDARDS OF THE PUBLIC COMPANY ACCOUNTING OVERSIGHT BOARD, Auditing Standard No. 1 (Pub. Co. Accounting Oversight Bd. 2003), *available at* http://pcaobus.org/Rules/Rulemaking/Docket010/2003-12-17_Release_2003-025.pdf, *archived at* http://perma.cc/Y4PK-8QBT.

400. AUDITOR INDEPENDENCE, R. 3520 (Pub. Co. Accounting Oversight Bd. 2006), *available at* http://pcaobus.org/Rules/PCAOBRules/Documents/Section_3.pdf, *archived at* http://perma.cc/SZK5-6S6Z.

401. *See* 15 U.S.C. § 78j-1(g)–(h) (2012) (listing these relationships).

402. 17 C.F.R. § 210.2-01(c)(4) (1999).

advisory services to audit clients.[403] By 2000 audit firm revenues derived from non-audit advisory services grew to 50% of total revenues where twenty years earlier non-audit fees had constituted only 13% of total revenues.[404]

There resulted a softening in auditors' positions regarding questionable accounting treatments employed by their clients.[405] Consider the audit of a company's internal control and monitoring systems. An auditor is unlikely to question the effectiveness of a compliance system sold by another division of his or her own firm. Yet, during the 1990s, auditing firms routinely sold compliance systems to their clients—for instance, Arthur Andersen, the audit firm that signed off on Enron's fraudulent financials of the late 1990s, had sold Enron its compliance system in 1993.[406]

The conflict bound up in auditor consulting closely resembles that bound up in a banker staple. The unconflicted banker is supposed to work hard to maximize value for the selling company's shareholders. As we have seen, a banker that stands to make more money as a lender to the acquiring company has an incentive to draw back and take a more accommodating posture.[407] Compare an unconflicted auditor, who is charged to maintain a posture of independence regarding its audit client[408] so as to position itself to impose Generally Accepted Accounting Principles (GAAP) despite the protests of the client's managers. An auditing firm that stands to make substantial money through ancillary consulting fees will lose this independent edge: better to keep the client's managers happy by passing on dubious accounting treatments than to alienate it by refusing a favorable opinion on its financials and thus lose consulting business.

Auditor consulting became a policy problem as the 1990s came to a close. The audit firms stoutly defended themselves and lobbied against new regulation.[409] The SEC, after much gnashing of teeth, in 2000 promulgated

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403. John C. Coffee, Jr., *What Caused Enron? A Capsule Social and Economic History of the 1990s*, 89 CORNELL L. REV. 269, 291 (2004).

404. John C. Coffee, Jr., *The Acquiescent Gatekeeper: Reputational Intermediaries, Auditor Independence and the Governance of Accounting* 27 (Columbia Law Sch. Ctr. for Law & Econ. Studies, Working Paper No. 191, 2001).

405. William W. Bratton, *Enron, Sarbanes-Oxley and Accounting: Rules Versus Principles Versus Rents*, 48 VILL. L. REV. 1023, 1030 (2003). For a similar discussion of auditor conflicts, see ***id.***

406. *See* Thaddeus Herrick & Alexei Barrionuevo, *Were Enron, Anderson Too Close to Allow Auditor to Do Its Job?*, WALL ST. J., Jan. 21, 2002, http://online.wsj.com/article/0,,SB1011565452932132000,00.html, *archived at* http://perma.cc/P3GZ-NEED (explaining that Enron became especially close with Arthur Andersen after it took over Enron's internal audit in 1993).

407. *See supra* text accompanying note 126.

408. CODIFICATION OF ACCOUNTING STANDARDS AND PROCEDURES, Statement on Auditing Standards No. 1, § 220.02 (Am. Inst. of Certified Pub. Accountants 1972).

409. RICK ANTLE ET AL., AM. INST. CERTIFIED PUB. ACCOUNTANTS, AN ECONOMIC ANALYSIS OF AUDITOR INDEPENDENCE FOR A MULTI-CLIENT, MULTI-SERVICE PUBLIC ACCOUNTING FIRM 24–25 (1997), *available at* http://ssrn.com/abstract=1466963, *archived at*

a rule that much lengthened the list of prohibited services, adding bookkeeping, financial information systems design, appraisal or valuation services, actuarial services, fairness opinions, and management functions.[410]

The new prohibitions came too late to forestall disaster. Enron, with its combination of sham transactions and antecedent (and lucrative) auditor consultation in the transactions' structure,[411] demonstrated that consulting relationships indeed contribute to catastrophic audit failures. In 2002 Congress embedded the substance of the SEC's rule in the Sarbanes-Oxley Act.[412]

2. Per Se Possibilities.—The per se approach taken to auditor conflicts by the SEC and Sarbanes-Oxley is a regulatory alternative open in any case where an advisory conflict holds out the possibility of negatively impacting a third-party interest.[413] Does a justification for outright prohibition of banker conflicts follow by analogy?

a. Broad-Brush Prohibition.—Broad-brush prohibition of banker conflicts holds out a few attractions. It would clear the scene of "appearance[s] of impropriety,"[414] thereby enabling (arguably) more reasonable sale processes. The selling board of directors would altogether avoid the cumbersome and risky business of managing conflicts. All it would need to do is engage an unconflicted banker, or, in cases of post-engagement conflicts, terminate the relationship and substitute an un-conflicted banker.

On reflection, however, absolute prohibition would not work well. There are four categories of concern: structural, shareholder-oriented, institutional, and policy based.

i. Structural.—As we saw in Part II, M&A is not a world of randomly selected, one-time buyers and sellers.[415] Banks, even boutique banks, are repeat players.[416] So are buy-side private equity firms and the banks that

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http://perma.cc/F9DX-W9MM (arguing that providing consulting services is not a threat to auditor independence).

410. 17 C.F.R. § 210.2-01(b) (2014).

411. Herrick & Barrionuevo, *supra* note 406.

412. Sarbanes-Oxley Act of 2002, Pub. L. No. 107-204, § 201, 116 Stat. 745, 771 (2002) (codified as amended at 15 U.S.C. § 78j-l (2012)). The section also requires preapproval by the reporting company's audit committee for any non-audit services not on the prohibited list. *Id.* § 201(h).

413. *See generally* Bratton, *supra* note 405 (arguing that, in the context of auditor conflicts, formal rules rather than agency-based duties should govern).

414. *In re* Toys "R" Us, Inc. S'holder Litig., 877 A.2d 975, 1006 (Del. Ch. 2005).

415. *See supra* text accompanying notes 109–110.

416. *See supra* text accompanying note 110.

finance cash deals.[417] Thus, even absent a staple, the bank representing a seller in a private equity buyout easily can have loans outstanding to companies owned by the private equity buyer and can be assumed to be making more loans to the buyer's investees in the future. Relationships develop as these institutions deal with one another repeatedly. It follows that a rule of absolute prohibition could have unintended, disruptive effects. A selling firm could have difficulty finding a completely unconflicted advisor with the wherewithal for the job. The Delaware courts recognize the problem: prior relationships between banker–advisors and private equity firms on the buy-side do not by themselves undermine a sale process.[418]

There is an argument in response: a broad-brush ban would precipitate beneficial industry restructuring—numbers of boutique firms limiting themselves to advising potential merger partners would grow to meet the resulting demand. The prediction is credible. We have seen that the sector is fluid and that talented bankers follow the bonuses.[419] Indeed, boutique market share has been growing in recent years.[420]

But industry structure holds out a rebuttal argument for the big banks, based on their ability to provide a full range of market information.[421] Some selling companies will make business judgments that they need real time input regarding market conditions in addition to the strategic advice on offer from a couple of experts who have hung out a shingle. To get an advisor with an infrastructure to provide this input, a large repeat player must be engaged. On this view of the world, recourse to a full service bank may be unavoidable given a large, complex transaction. We should accordingly leave boards of directors with a zone of discretion for managing conflicts.

It also bears noting that the system not only tolerates conflicts but goes out of its way to create them. The standard performance fee creates a conflict by incentivizing the banker to favor a less risky low price over a more risky higher price,[422] and alternative fee structures could ameliorate the problem. Commentators have been criticizing the practice for more than two decades.[423] Yet the fee arrangements remain unchanged, presumably because the clients prefer them.

417. *See supra* text accompanying note 110.

418. *See In re* Dollar Thrifty S'holder Litig., 14 A.3d 573, 581–82 (Del. Ch. 2010) (stating that a prior relationship between a banker–advisor and a private equity firm on the acquiring side is simply "one of the facts of business life").

419. *See supra* text accompanying notes 154–155.

420. *See supra* text accompanying note 152 and Figure 1.

421. *See supra* notes 88–91 and accompanying text.

422. *See* Kisgen et al., *supra* note 59, at 185 (noting that contingent fees can prompt advisors to push for bad deals).

423. *See supra* note 193.

Auditing conflicts can be distinguished at this point: self-interested managers have every reason to create auditor conflicts so as to compromise independence toward the end of increasing management's discretion regarding accounting treatments.[424] There is no comparable perverse incentive in sale contexts, at least absent a particular self-interested tie to the buyer on the sell-side board.

ii. Shareholder Benefits.—Shareholder interests may be best served by a full-service bank with built-in conflicts. Merger-advisory services are about information and a bank with which management has a long-term relationship knows more about the company. That edge easily can trump dangers stemming from personal relationships from sell-side managers.

Even buy-side relationships may fall short of disabling when all costs and benefits are tallied. Hypothesize a strategic merger with a same-industry buyer. There happens to be one banker who knows the industry better than any other, a banker with unique knowledge and skills who for many years has advised many companies in the industry on mergers and other strategic choices. This banker comes to the selling company having advised the purchasing company in the past and has a present expectation of providing the purchaser with future services—a clear conflict. Yet the selling company may be better off with the conflicted banker on its team, both to secure the best informed advice and to prevent the best informed advisor from joining the opposing team. Arguably, the selling board reasonably can manage the conflict, engaging a second bank to provide the fairness opinion and disclosing the conflict to its shareholders.

In sum, expected shareholder benefits can figure importantly and reasonably into the calculations of sell-side boards that tolerate banker conflicts. A heavy presumption against per se regulatory intervention follows.

iii. Institutional.—Even if we were to determine that a broad-brush prohibition makes cost–benefit sense, the Delaware Chancery Court is not the lawmaker equipped to lay down the mandate. The exercise is legislative: terms need to be defined and lines need to be drawn; formal regulations drafted by experts are the best means to that end.

Assuming that regulations are desirable, what body should do the formulating? By analogy to other professions, a self-regulatory organization should generate rules on conflicts along with best practice guidelines for advisors and givers of fairness opinions—a banker's equivalent of the American Institute of Certified Public Accountants or the American Bar

424. *See* Bratton, *supra* note 395, at 442 (describing the problem as one of managers "cross[ing] the auditors' palms with silver in exchange for a free hand to manage bottom-line numbers").

Association. But there is no organization that functions in this way.[425] But, where lawyers and auditors long ago organized as guilds, chilling competition and regulating themselves into the bargain, investment banks have refrained from doing so.[426] Perhaps selling boards and their shareholders would be better off if investment banks had evolved differently; perhaps FINRA should lower the boom on the banks and mandate professional organization. Such an intervention implies a fundamental change of approach, fundamental enough to make it unreasonable to look to Delaware corporate law as the leading edge of change.

iv. Policy.—Fundamental reform follows from recognition of a fundamental structural problem. It is not at all clear to us that banker conflicts have this salience. One study looks to see if acquisition premiums are sensitive to investment banker fee structures.[427] It finds no evidence that fee structure drives premiums—the drivers instead are target and transaction characteristics, with which the fees do vary.[428]

Nor does anyone make a broader claim that sale processes are so skewed against seller shareholders as to cause them to be systematic losers. Merger premiums are substantial, so substantial as usually to arrogate the merger gain to the target shareholders. Studies of announcement period price effects bear out this assertion with a stark allocational picture.[429]

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425. For a proposal of an Investment Banking Authority that would issue guidelines and standards, see Davidoff, *supra* note 35, at 1615–19.

426. *See* John C. Coffee, *Limited Options*, LEGAL AFFAIRS, Nov.–Dec. 2003, http://www.legalaffairs.org/issues/November-December-2003/review_coffee_novdec03.msp, *archived at* http://perma.cc/ZNZ6-R6SB ("Accountants . . . and attorneys all belong to self-regulating professions. Much like medieval guilds, [these] professions regulate themselves protectively," but "time will tell . . . whether professional independence is even a realistic goal for the 'sell-side' analyst").

427. Calomiris & Hitscherich, *supra* note 55, at 9–10.

428. *Id.* There are a number of other studies of bankers and fees. Results are inconclusive. *See* Helen M. Bowers & Robert E. Miller, *Choice of Investment Banker and Shareholders' Wealth of Firms Involved in Acquisitions*, 19 J. FIN. MGMT., Winter 1990, at 34, 37, 39 (addressing the relationship between acquisition fees and shareholder wealth in an empirical study analyzing whether the choice of investment banker affects shareholder wealth); William C. Hunter & Mary Beth Walker, *An Empirical Examination of Investment Banking Merger Fee Contracts*, 56 S. ECON. J. 1117, 1118 (1990) (finding a positive relationship between banker fees and social gain in merger transactions); Rau, *supra* note 149, at 322 (studying incentive fee structures and finding that the difference in fee structures relates to market share); Anthony Saunders & Anand Srinivasan, *Investment Banking Relationships and Merger Fees* 3 (NYU Stern Sch. Bus. Research Series, Working Paper No. S-FI-01-07, 2001), *available at* http://papers.ssrn.com/sol3/papers.cfm?abstract_id=1298849, *archived at* http://perma.cc/V9F2-Y5GH (determining that buy-side firms pay higher advisory fees to advisors they have long-term relationships with without experiencing significantly better results).

429. Studies of fairness opinions add an intriguing fact—while sell-side fairness opinions have no effect on premium or announcement period return, in the one-third of cases where the buyer gets a fairness opinion, premiums are 4.3% lower but buyer announcement period returns are also 2.3% lower. Kisgen et al., *supra* note 59, at 180.

While target shares go up a consistent 16% during the three days surrounding announcement, bidder shares go down—the average was −0.3% in the 1970s, −0.4% in the 1980s, and −1.0% in the 1990s.[430] Over a time window of several months, target shares average an increase of 23.8%, while bidder shares on average go down around 4%.[431] The figures imply consistent losses to bidder shareholders.[432]

The policy implication is straightforward: *Revlon* has been working well for the sell side.

Summary.—The four grounds of objection cumulate to rebut the proposition that broad-brush prohibition of banker conflicts would materi-ally improve the platform on which companies are sold.

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430. Gregor Andrade et al., *New Evidence and Perspectives on Mergers*, J. ECON. PERSP. 103, 110 tbl.3 (2001).

431. *Id.* The decline was –4.5% in the 1970s, –3.1% in the 1980s, and –3.9% in the 1990s. *Id*. There is a literature that sorts for the characteristics of bidder firms with low abnormal returns. Sara B. Moeller et al., *Wealth Destruction on a Massive Scale? A Study of Acquiring-Firm Returns in the Recent Merger Wave*, 60 J. FIN. 757, 770 (2005), summarizes its results as follows: abnormal returns are lower for (1) low leverage firms; (2) low Tobin's *q* firms; (3) firms with large cash holdings; (4) firms with low managerial ownership of shares; and (5) large capitalization firms. Lower abnormal returns are also associated with certain transactions: (1) public firm targets; (2) target opposition; (3) conglomerate results; (4) competitive bidding; and (5) stock consideration. *Id.* at 770–71.

432. A reference to portfolio theory makes the results less disturbing. Most bidder shareholders own their shares in diversified portfolios. They thus stand on both sides of the deal and so are indifferent to the division of gain as between bidder and target. Robert G. Hansen & John R. Lott, Jr., *Externalities and Corporate Objectives in a World with Diversified Shareholders/Consumers*, 31 J. FIN. & QUANTITATIVE ANALYSIS 43, 59 (1996). So long as the combined result for the bidder and the target nets out positive, everything is fine. And such was the case until the late 1990s: from 1973 to 1998, the combined three-day-window result averaged a positive 1.8%; from 1973 to 1979, the average was 1.5%; from 1980 to 1989, the average was 2.6%; and from 1990 to 1998 the figure was 1.4%. Andrade et al., *supra* note 430.

Unfortunately, a cluster of mergers in the late 1990s reversed the 1.8% long-term positive. Sarah Moeller, Frederik Schlingemann, and René Stulz marshal some shocking three-day announcement returns. They show that from 1980 to 1990, bidder firms' shares lost an aggregate $4 billion, and from 1990 to 1997 they gained $24 billion. Moeller et al, *supra* note 431, at 758–59. From 1998 to 2001, however, they lost $240 billion, bringing down the 1990 to 2001 result to a $216 billion bidder loss. *Id.* The 1998 to 2001 numbers are so bad that they make for a negative combined result of $134 billion for bidders and targets in the period. *Id.* The negative dominoes fall from there. Where in the 1980s combined returns were a positive $12 billion, from 1991 to 2001 the combined loss was $90 billion. *Id.* at 763. That nets out to a $78 billion loss for 1980 to 2001.

These disastrous results stem from 87 deals out of a total of 4,136 in the authors' sample. *Id.* at 765. The large-loss deals were more likely to be hostile tender offers and more likely to be in the same industry, but neither result is statistically significant. *Id.* at 771. The most prominent common feature among the bidding firms is prior acquisition behavior. They are serial acquirers with high market valuations that in the past had made value-enhancing acquisitions. *Id.* at 777. Moeller, Schingemann, and Stulz suggest that the pattern of success causes an increase in the managers' zone of discretion. *Id.* The managers then push the acquisition pattern too far and the market withdraws its support. *Id.* at 777–78.

b. Narrow and Tailored Prohibition.—Let us suppose that Vice-Chancellor Strine had been tougher in *Toys "R" Us*—that instead of disavowing any intent to make a "bright-line statement"[433] in the case he had gone ahead and done so, holding that targets seeking to pass *Revlon* inspection must avoid staples.

A narrowly framed staple remover would avoid many of the problems that beset the broad-brush prohibition hypothesized above. Definitional problems would be minimal and the case for judicial competence would be stronger. Interference with pricing arrangements and other market practices also would be minimal. Such a prohibition still would cut against the grain of *Revlon* jurisprudence. In its earliest iterations, *Revlon* was thought to have a bright-line aspect, requiring an open auction.[434] The Delaware courts smoothed that rule-like aspect out over time, calling only for the realization of the "highest value reasonably attainable" without specific directives as to the means to the end.[435] *Revlon* is very much a standard.

A staple-remover also triggers questions concerning the sell-side shareholder interest. We have seen that staples have defenders and that the arguments in favor work well as regards the auction of a privately-held company.[436] But a shareholder-beneficial staple is easily hypothesized even outside of that narrow auction framework. This time Target, Inc.'s managers take a look at their industry and decide that the time has come to sell. They engage Unibank, their longtime banker–advisor, and sit down with it and work out an upset price. Unibank shops the company with little success on the strategic side. But a financial bidder meets the upset price and, with a little negotiation, exceeds it. Credit is tight and the buyer has trouble putting together a banking syndicate. It becomes clear during the negotiation process that Unibank's participation will be necessary.

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433. *In re* Toys "R" Us, Inc. S'holder Litig., 877 A.2d 975, 1006 n.46 (Del. Ch. 2005).

434. *See* Barkan v. Amsted Indus., Inc., 567 A.2d 1279, 1286 (Del. 1989). Rejecting this bright-line approach, the Supreme Court of Delaware stated in *Barkan v. Amsted Industries*:

> This Court has found that certain fact patterns demand certain responses from the directors. Notably, in *Revlon* we held that when several suitors are actively bidding for control of a corporation, the directors may not use defensive tactics that destroy the auction process. When it becomes clear that the auction will result in a change of corporate control, the board must act in a neutral manner to encourage the highest possible price for shareholders. However, *Revlon* does not demand that every change in the control of a Delaware corporation be preceded by a heated bidding contest. *Revlon* is merely one of an unbroken line of cases that seek to prevent the conflicts of interest that arise in the field of mergers and acquisitions by demanding that directors act with scrupulous concern for fairness to shareholders.

Id. (citations omitted).

435. Mills Acquisition Co. v. Macmillan, Inc., 559 A.2d 1261, 1288 (Del. 1988); *see also Barkan*, 567 A.2d at 1286 ("[T]here is no single blueprint that a board must follow to fulfill its duties. A stereotypical approach to the sale and acquisition of corporate control is not to be expected in the face of the evolving techniques and financing devices employed in today's corporate environment.").

436. *See supra* notes 99–107 and accompanying text.

Unibank, as Target's longtime advisor, knows more about its internal operations than any third party. Its participation in the bank syndicate imports outcome-determinative informational credibility.[437] A per se rule against staples kills a good deal.

3. Summary.—We began this section asking why banker conflicts are tolerated where auditor conflicts are not. The answer lies in accumulated experience. Severe auditor conflicts were once tolerated even though the context was professionalized and auditors owed clear fiduciary duties to their clients. Discomfort among federal regulators grew as the conflicts became more severe. Ultimately, audit failure combined with financial disaster to lead to hardwired prohibitions in Sarbanes-Oxley. Banker conflicts in merger negotiations present much less of a threat to investor interests than did the auditor conflicts of the 1990s. The value of the service rendered does not depend on independence. Any taints or skews are transaction specific. With auditing, in contrast, the stakes go to the informational integrity of the entire stock market. Mergers, moreover, particularly activate boards of directors. The board, which normally sits back and monitors, moves to the forefront of day-to-day decision making, better enabling it to manage advisor conflicts effectively. Finally, banker conflicts have been subject to scrutiny in the Delaware courts since the day *Revlon* was decided. This backstop, case-by-case supervision makes it unlikely that these relational compromises will lead to a systemic breakdown in governance processes, as happened with auditor conflicts.

B. Safe Harbor

Subpart A took up the claim that *Del Monte* and *El Paso* stop too short in their policing of banker conflicts, looking into the possibility of a fresh, prohibitive approach. As it happened, none of the per se alternatives posed emerged as obviously superior to *Revlon* scrutiny. This subpart takes up the other side of criticism of *Del Monte* and *El Paso*—the claim of regulatory boundaries overstepped, looking for a bright-line rule that might qualify conflicted representation. We couple the disclosure rule with the solution derived in practice to qualify staples in the wake of *Toys "R" Us*,[438] positing that full disclosure to the selling board and the shareholders taken together with engagement of a second, unconflicted banker circumstantially guarantees a clean deal. The proposition is sensible. But whether the circumstantial guarantee suffices to justify the creation of a safe harbor to

437. *Cf.* Linda Allen et al., *The Role of Bank Advisors in Mergers and Acquisitions*, 36 J. MONEY CREDIT & BANKING 197, 200 (2004) (empirically confirming a positive "certification effect" in cases where a commercial bank served as merger advisor).

438. *See supra* notes 255–260 and accompanying text.

immunize banker–client relationships from later *Revlon* disruption still presents a difficult question. We conclude that it does not.

1. *The Case in Favor*.—We use the term "safe harbor" loosely, for in our standards-based regime of corporate fiduciary law, no conflicted transaction can be shielded with 100% certainty. That said, safe harbors are not unknown in corporate fiduciary law—a famous one obtains in respect of director and officer self-dealing transactions. In Delaware, majority disinterested-director approval based on full disclosure blocks *ex post* judicial scrutiny for fairness and triggers the protection of the business judgment shield.[439] By analogy, full disclosure of banker conflicts to sell-side boards and shareholders could have a similar effect with *Revlon* scrutiny. To the extent that a conflict could still impair the sale process, engagement of a second banker holds out additional comfort, with the two together operating as a safe harbor.

Full disclosure and second banker engagement already provide substantial insulation on the narrow question whether a banker conflict undercuts a fairness opinion.[440] We only carry this usage to its logical conclusion in the following affirmative restatement: full disclosure plus independent director approval plus resort to a second banker together block a *Revlon* claim grounded in tainted banker influence.

A question arises at the outset. Why include the third leg of second banker engagement, and why not impart safety based on a basic agency law approach: full disclosure and informed consent subject to a bad faith backstop? The parties are sophisticated and the bad faith backstop leaves a considerable stretch of conflicted territory remaining outside the ring of safety. The *Del Monte* fact pattern, for example, gets no protection here; when the banker deceives the client disclosure is anything but full and bad faith is clear.

The second banker does address an important problem. The conflicted advisor deals with counterparties outside of the board's purview and recommends actions from a position of informational superiority. This stretches the consenting board's monitoring capabilities to the limit. It is not hard to posit a situation where the conflict impairs the process despite full disclosure and consent. The buy-side ownership interest in *El Paso* arguably presents such a case. Second banker engagement addresses the problem: the board retains what it values in the conflicted banker's participation while assuring a flow of unconflicted advice, easing the monitoring burden. A second banker requirement makes the safe harbor

439. DEL. CODE ANN. tit. 8, § 144(a) (2011); *see also* Benihana of Tokyo, Inc. v. Benihana, Inc., 891 A.2d 150, 173–75 (Del. Ch. 2005), *aff'd*, 906 A.2d 114 (Del. 2006) (applying the "safe harbor" provision of § 144(a) and noting that one director's interest in the transaction "would not vitiate the presumptions of the business judgment rule").

440. *See supra* notes 188–93 and accompanying text.

less capacious while providing a stronger assurance that the conflict will be mediated successfully. As such it adds robustness to the proposal.

The safe harbor also would impart added certainty to sell-side actors, and it would have the advantage of being optional—a board not wishing to engage a second banker could take a pass, accepting the risk of subsequent *Revlon* litigation. A safe harbor would also make it harder for plaintiffs, an attractive result in an era when the fact of a sale by itself makes a court challenge highly probable.[441] The trend toward merger litigation makes *Del Monte* and *El Paso* look inopportunely timed, dumping grist at a shabby litigation mill. It arguably is time to cut back on the size of the playing field.

2. Contrary Concerns.—The utility of the safe harbor just posited suffers from significant practical limitations. First, any effect on the overall burden of *Revlon* litigation would be nominal, for a safe harbor concerning banker conflicts would not shut the *Revlon* door. It would only foreclose one line of scrutiny within a wider inquiry and then only after a determination that full disclosure actually had been made, a conclusion likely to be subject to plaintiff challenge. Second, there would be a problem of specification. Second banker engagement implies mediation: the board must decide what tasks go to the new banker and what tasks remain with the old one. *El Paso* presented a case where a problem persisted despite such a division of labor.[442] To hold out review of the specification denudes the safe harbor of value. If a plaintiff attacks the appropriateness of the deployment of the two bankers as well as the disclosure, then the defending board ends up in substantially the same position as in a world without a safe harbor. Of course, the safe harbor's value could be preserved with a blunt approach: so long as a second banker comes on board, safety is achieved no matter how the board deploys the two bankers. But this is a large concession, so large as to make one wonder whether the substantive cost of a safe harbor outweighs the benefits. Third, there is a question regarding out-of-pocket cost, second banker engagement being an expensive expedient. Maybe the shareholders would be better off in the long run under a stricter regime that pushes boards in the direction of engagement severance.

Finally, there is a question regarding the magnitude of the certainty enhancement. Banker conflicts crop up as troublesome facts in the course of a broader inquiry into the sale process. A safe harbor in effect tells the inquirer that the fact no longer should be deemed troublesome. The resulting effect on the inquiry as a whole is hard to project. Presumably, a

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441. In 2005, 39.3% of closed deals in Professors Cain and Davidoff's dataset experienced state law litigation; by 2011, the figure rose to 92.1%. Cain & Davidoff, *supra* note 13, at 3.

442. *In re* El Paso Corp. S'holder Litig., 41 A.3d 432, 434 (Del. Ch. 2012).

safe harbor would cut off a claim based exclusively on a banker conflict taint and alleging that the banker's compromised incentives by themselves made the sale process unreasonable without alleging any more particular negative effects. A showing of particular effects would present a line-drawing problem. Assume for example, a safe-harbored conflict along with independent facts showing that the banker skewed a competitive sale process toward a favored bidder. The skew, although a consequence of the conflict, presumably would remain a legitimate topic of inquiry, problematizing the banker's performance and incentives despite safe harbor protection.

There is also a question concerning the allocation of the burden of uncertainty. Boards of directors already possess a straightforward expedient with which to deal with severe banker conflicts—prohibition. They look to counsel to determine whether the conflict requires that drastic step.[443] If, once advised of litigation risk, the board chooses to continue with a conflicted banker because it values the relationship net of the conflict, the burden falls again on counsel, this time for a persuasive articulation of reasons and advice on appropriate contractual adjustments. Were a safe harbor to diminish this stress, counsel would be the primary beneficiary.

It is not at all clear to us that the corporate lawyers who give this advice need this solicitude. This is a variant of the standards versus rules debate,[444] with *Revlon* as the judicially administered, open-ended standard and the proposed safe harbor as a modifying rule. Standards assure that the regime of scrutiny covers all fact patterns at the cost of a high compliance burden on regulated parties. Rules relieve the burden by holding out specific instructions at the cost of regulatory arbitrage in the form of compliant conduct that subverts the regulatory objective.[445] The case for rules strengthens as the volume of regulated traffic increases and proximity of scrutiny decreases, as with GAAP and federal securities disclosure requirements.[446] In these situations, precise instructions save costs, and rules as a practical matter may be the only effective mode of regulation. Bankers and boards present the opposite situation. In public company governance, sale processes are the exception not the rule;[447] multiple parties

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443. *Cf.* HAZARD ET AL., *supra* note 216, § 11.20 (reflecting that, when an attorney's own conflict is at issue, such conflict may be so severe as to be "non-consentable").

444. *See generally*, Louis Kaplow, *Rules Versus Standards: An Economic Analysis*, 42 DUKE L.J. 557, 559–60 (1992) (describing the standards-versus-rules debate as one emphasizing whether law is given substance *ex post* or *ex ante*, respectively).

445. *Cf.* William W. Bratton, *Rules, Principles, and the Accounting Crisis in the United States*, 5 EUR. BUS. ORG. L. REV. 7, 30–33 (2004) (detailing the benefits of rules in the accounting context).

446. *Cf. id.* at 30 (arguing that "[t]he case for rules strengthens materially in an imperfect institutional framework, such as that prevailing respecting the audit function in the US").

447. *See* Christina M. Sautter, *Promises Made to be Broken? Standstill Agreements in Change*

weigh in carefully on important decisions and given a challenge, scrutiny will be close. There is no analogy to wholesale matters like GAAP and federal securities compliance. In other words, merger sale process is the archetypical case for a standard. In a one-off, big-money context, claims of a need for guidance or safety should be deeply discounted.

3. Conclusion.—We doubt that our hypothesized safe harbor makes cost–benefit sense. To dredge a safe harbor is to value litigation certainty over the risk of sale process infirmity. We would not make that choice, absent a showing that indiscriminate filings by the plaintiffs' bar have driven the cost of *Revlon* scrutiny to unacceptable heights. We do not read recent litigation statistics to signal a law reform as anything approaching such an emergency.

C. Commentary

Our double-barreled search for alternative approaches returns us to the starting point: judicial scrutiny under the open-ended *Revlon* standard. If our analysis is persuasive, it implies the conclusion that there is no clearly superior alternative to *Revlon* scrutiny despite the attendant risks and uncertainties.

VI. Conclusion

Robert Kindler, a banker at Morgan Stanley, has been quoted as saying, "We are all totally conflicted—get used to it."[448] What is he telling us? He could be making a structural point: because the banking sector is concentrated, conflicts are inevitable and accordingly must be tolerated and their management left to the client's discretion. He could be making a relational point: because banker–advisors are not really fiduciaries, conflicts are permitted and accordingly should be tolerated and managed. He could be making both points. Whatever Mr. Kindler's more particular communicative motivation, he makes one thing absolutely clear: bankers themselves are untroubled by conflicts and have no incentive to ameliorate any resulting problems through self-regulation.

With *Del Monte* and *El Paso* the Delaware Chancery Court "gets used to it." But, contrary to Mr. Kindler's implication, familiarity does not result in acceptance. Importantly, the court's treatment of banker conflicts does not follow from a revitalization of the dormant, fiduciary side of the

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of Control Transactions, 37 DEL. J. CORP. L. 929, 942–43 (2013) (recognizing that "not every sale requires a full-blown auction process" and corporate boards can opt for more limited negotiated sales rather than public auctions).

448. Andrew Ross Sorkin, *When a Bank Works Both Sides*, N.Y. TIMES, Apr. 8, 2007, http://www.nytimes.com/2007/04/08business/yourmoney/08deal.html, *archived at* http://perma.cc/SA36-QFQ9.

banker–client relationship. The banker fiduciary duty has not awakened, reared its head, and started roaring about honor and self-sacrifice. *Revlon* is about the board's unquestioned, unwaivable fiduciary duty to the shareholders. Whether or not the banker should or should not have done something is irrelevant. The question is whether the board, in contracting mode, should have permitted or contained it. There is no clash between contractual and fiduciary values; this is all on the contractual side.

But, even as these cases apply the law without changing its terms, the M&A world looked very different before than it does after. Before, the law of banker–client relationships amounted to a field open to contracting out subject to minimal *ex post* scrutiny. After, there is a cognizable potential for reasonableness review. Before, shareholders had no tractable cause of action against a banker. After, a shareholder action under *Revlon* can effect forfeiture of the banker's fee and contribute to an attractive return to a class action attorney, while a robust aiding and abetting claim can hold out a money judgment jackpot.

Why, if the possibility for intervention against banker conflicts lay inherent in the structure of *Revlon* inquiry, did it take so long for intervention to occur? Perhaps the delay was just an accident of history—no case happened to come along. But maybe more has been going on. Relational standards may have declined over time, with cognizable conflicts finally showing up amidst the stress of a severe recession. Evidence of increasing bank concentration taken together with the reactive rise of the boutique sector[449] support this reading. Perhaps the Chancery Court became more sensitive to banker incentive problems, influenced by the widespread skepticism about practices at big banks triggered by the financial crisis.[450] If so, the change is a legitimate one: like a banker, the Chancery Court has a reputation to protect.

In any event, changes which loom large in the *Revlon* context look less than fundamental when we take a step back and look at M&A as a whole. The Chancery Court's interventions are discreet and occur as a phase of the deal-making process. The challenged mergers still closed and actors on Wall Street labor under no per se conflicts prohibition. Primary decision making is still remitted to the board of directors of the banker's client. The cases simply shift the cost–benefit calculus against the bankers. And, even as the cases also enhance the authority of the lawyers in the sell-side team's internal discussions, the decision remains a business rather than legal judgment, in this case exercised by independent directors.

449. *See supra* notes 86–87 and accompanying text.

450. We note that the spike in boutique market share in the down market of 2008 has been attributed to reputational reverses at commercial banks in the wake of the financial crisis. Jessica Silver-Greenberg, *Boutique Banks to Cash In*, BLOOMBERG BUSINESSWEEK, Sept. 23, 2008, http://www.businessweek.com/stories/2008-09-23/boutique-banks-to-cash-inbusinessweek-business-news-stock-market-and-financial-advice, *archived at* http://perma.cc/X396-2WXK.

Perhaps banker–client relationships should be considered de novo with a view to articulation of best practices, whether at the instance of bankers undertaking formal organization as a profession or the existing self-regulatory organization, FINRA, imposing client duties on bankers as an incident of market regulation. Such a fundamental relational restructuring could not be undertaken effectively by the Delaware courts. To the extent the Chancery Court's minimalist but high profile interventions forestall such fundamental reform initiatives by diminishing the volume and magnitude of banker conflicts, the bankers owe the court a word of thanks.