

5c: case analysis



Case Analysis: Gries Sports Enterprises, Inc . V. Cleveland Browns Football Co., Inc. Introduction: This case discusses two doctrines of corporate law: The Business Judgment Rule and the Fairness Rule, in connection with the roles, responsibilities and duties of the directors as well as the shareholders of the companies involved. The parties discussed in this case include, The Gries Sports Enterprise Inc, Cleveland Browns Football Co. Inc and the Cleveland Stadium Corporation. The various arguments and counter arguments put forward in this case as well as the court's ruling shed light on the various business and legal aspects of the two significant doctrines mentioned above.

Facts of the case:

Arthur Modell, a majority shareholder of Cleveland Browns Football Co., Inc as well as the Cleveland Stadium Corporation along with James Bailey, the secretary and general council of CSC, as well as chief counsel of Cleveland Browns Football Co., Michael Poplar, the Chief Financial Officer of CSC, and James Berick, the shareholder of CSC as well as outside counsel and shareholder of Cleveland Brown Football Co., Inc appraised the price of CSC and made a purchase decision which was perceived to be overvalued by the other minority shareholders Gries and Cole, who moved to court to seek appealing against the opportunistic directors and the subsequent injustice caused and seeking fairness by over ruling the business judgment rule that often seeks to protect the fairness of the decisions made be the directors.

Q1. Which party had the burden of proof in this case?

According to the business judgment rule, the burden of proof lies on the employee / plaintiff / the party challenging the decision of the board of directors. In this case the burden of proof lied on Gries Sports Enterprises.

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But on removal of the protection of the business judgment rule by the trial court, whereby the judgment of the court of appeals was reversed and reinstated, the burden of proof was shifted to the accused, in this case, the Cleveland Browns Football Co., Inc.

2. According to the courts opinion, what factors should be taken into consideration in determining whether a director has an interest in a transaction that is challenged by a shareholder in a derivative lawsuit?

The following factors should be taken into consideration:

The director would be considered as having an express interest in a transaction if either of the following factors is satisfied:

- i. He appears on both the sides of the transaction
- ii. He has or expects to derive a personal financial benefit not equally received by the stakeholders

3. According to the courts opinion, when is a director independent, and under what circumstances does the director lose that independence?

A director would be considered as independent if his decision is based on the corporate merits of the subject before the board rather than extraneous considerations or influences.

He would lose that independence if he is found to be dependent on or dominated by or beholden to another person through personal or other relationship.

NOTE: the order details suggest that ATLEAST 3 of the questions listed should be answered. I have answered the required number of questions and as a compensation and a gesture of gratitude for your patience and co-operation, extended to me, I am including the answers to the remaining questions as well. Hope, that helps.

4. What circumstances does the court say will make a director informed?

According to the court's ruling on the matter, a director would be considered as "informed" if he makes a reasonable effort to become familiar with the relevant and reasonably available facts prior to making a business judgment.

5. When the business judgment rule cannot be used, as occurred in this case, what standard is applied by the court to determine whether to reverse a challenged decision made by the directors?

The business judgment rule cannot be used in the following circumstances:

The director is required to be independent, disinterested and informed in order to seek protection under the business judgment rule. In case of failure of satisfying any of the three factors, the protection would be removed whereby the fairness of the decision would be investigated and challenged by the court.

To determine whether to reverse a challenged decision the court looks at the three key elements, as mentioned above, that protect the fairness of the director's decision. If the director fails to satisfy any one of the three elements then the protection made available to the director under the business judgment doctrine would be removed and the court would then seek to investigate into the fairness of the decision on the basis of several other factors, failing of which would enable the court to reverse their decision against the favor of the directors.

6. Did the court consider the purchase of the Cleveland Stadium Corporation by the Cleveland

Browns to be fair to the corporation and the minority shareholders in this case? Why or why not?

No. The decision to purchase the Cleveland Stadium Corporation wasn't considered to be fair by the court since the directors failed to satisfy any of the conditions stated in the law that would have ensured them protection against such challenge. The court on applying the fairness rule, found the directors, Modell, Bailey, Poplar and Berick to be in an influential position whereby the control of making a transaction as well as fixing various terms related to the contract (such as pricing) was totally biased in their favor. Also there was a serious lack of any negotiations regarding the price, and other elements specific to the contract. Besides, the manner in which the subject transaction was initiated, structured and disclosed to plaintiffs therefore did not satisfy the reasonable concept of fair dealing.