RICHARDS LAYTON & FINGER

RECENT DEVELOPMENTS IN DELAWARE LAW

SPRING 2016

RICHARDS, LAYTON & FINGER, Delaware's largest firm and one of its oldest, has been committed from its founding to helping sophisticated clients navigate complex issues and the intricacies of Delaware law. Our lawyers have been involved in drafting many of the state's influential business statutes, and we have helped shape the law through our work on landmark cases decided in the Delaware courts. Our commitment to excellence spans decades and remains central to our reputation for delivering extraordinary counsel to our clients.

Introduction

WE ARE PLEASED TO PROVIDE RICHARDS LAYTON CLIENTS AND FRIENDS with this publication, which highlights recent corporate and alternative entity cases and statutory developments in Delaware. This publication continues our long tradition of providing insight into the development of Delaware law. Our attorneys have provided our clients with a concise quarterly update on Delaware law for more than two decades. In recent years, this update has been accompanied by a quarterly video, which allows clients and friends of the firm to gain insight into recent decisions and to ask questions of our attorneys. If you have not had the opportunity to receive our quarterly updates or participate in our video conferences, please let one of us know or send a note to corporate@rlf.com.

While time has altered how we relay information, Richards Layton retains a unique ability to offer insight and counsel on Delaware corporate law. Our corporate and alternative entities teams, the largest and most recognized in the state, play a crucial role in Delaware. For decades, we have contributed to the development of key statutes, litigated the most influential decisions, and provided counsel on the most sophisticated transactions. In 2015 our lawyers were deeply involved in drafting our state's innovative new arbitration legislation, the Delaware Rapid Arbitration Act, which offers a new option for efficient and binding resolution of business disputes.

Our lawyers continue to expand our deep understanding of Delaware law. We have been intimately involved with many of the cases highlighted in this publication, and we have handled, as Delaware counsel, the most merger and acquisition transactions valued at $100 million or more for 16 years running, as reported in *The Deal and Corporate Control Alert.* We welcome the opportunity to discuss the practical implications of these recent developments in Delaware law with you, and we look forward to helping you whenever a need may arise.

—Richards, Layton & Finger

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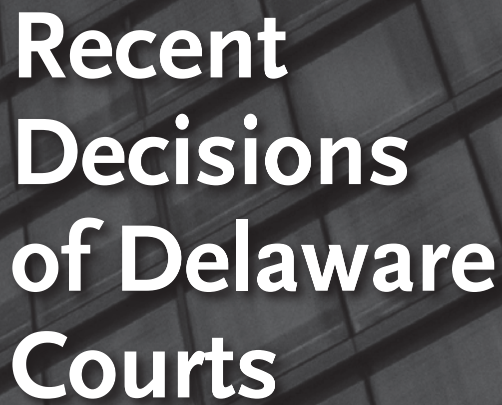

BUSINESS COMBINATIONS

Breach of Fiduciary Duty

In re EZCORP Inc. Consulting Agreement Derivative Litigation, 2016 WL 301245 (Del. Ch. Jan. 25, 2016).

In *In re EZCORP Inc. Consulting Agreement Derivative Litigation,* 2016 WL 301245 (Del. Ch. Jan. 25, 2016), the Court of Chancery denied a motion to dismiss derivative claims challenging a series of payments between a corporation and its controlling stockholder, even though those payments had been approved by the audit committee of the corporation's board. After review of extensive case law, the Court concluded that the weight of authority called for application of the entire fairness standard at the pleading stage, with the possibility that an evidentiary showing of independent committee approval could support a shift in the burden of proof later in the case. The Court determined that such transactions could be subject to dismissal at the pleading stage under the business judgment rule only where the transaction is approved by both an independent committee of the board and a majority of the minority stockholders.

Headquartered in Austin, Texas, EZCORP Inc. ("EZCORP" or the "Company") provided instant cash solutions through a variety of products and services, including pawn loans, other short-term consumer loans, and purchases of customer merchandise. The plaintiff stockholder brought suit challenging the fairness of three advisory service agreements between the Company and defendant Madison Park, LLC, an affiliate of the Company's controlling stockholder, Phillip Cohen. Cohen was the sole stockholder of the general partner of the limited partnership that held all of the Company's voting common stock. Thus, Cohen held 100% of EZCORP's voting power, but only 5.5% of its equity.

In May 2014, the audit committee terminated the renewal of one of the service agreements, allegedly due in part to the committee's concern about the fairness of the relationship between the Company and Madison

Park. In early July, the stockholder-plaintiff made a demand under Section 220 of the Delaware General Corporation Law to inspect the Company's books and records relating to the service agreements. Nine days after the books and records demand arrived, Cohen responded to the termination by removing three directors (including two members of the audit committee that had terminated the agreements and the Company's CEO) from the board; another director resigned the same day.

The Court considered at length the appropriate standard of review for transactions in which a corporation's controlling stockholder receives a non-ratable benefit. The Court noted that, in an ordinary case involving self-dealing between a corporation and its controlling stockholder, the standard of review is entire fairness and the burden of proof rests on the defendants. However, in the context of a cash-out merger, the Delaware Supreme Court has held that application of the business judgment rule is appropriate if, but only if, the transaction is conditioned *ab initio* on both the affirmative recommendation of a sufficiently authorized, independent and disinterested committee of the board and the affirmative vote of a majority of the minority stockholders. *See Kahn v. M & F Worldwide,* 88 A.3d 635 (Del. 2014). If the controlling holder agrees to use only one of these protections, however, "then the most that the controller can achieve is a shift in the burden of proof such that the plaintiff challenging the transaction must prove unfairness."

The Court then considered a controversy posed in the case law: whether challenges to controlling-stockholder transactions other than cash-out mergers may be dismissed under the business judgment rule where the transaction is conditioned on *either* approval by an independent and disinterested board committee *or* approval by a majority of the minority stockholders, but not both. After an extensive review of cases taking both sides of that issue, the Court concluded that the weight of the authority called for a broader application of the entire fairness framework.

The Court also considered the tension between that conclusion and the demand futility analysis articulated in *Aronson v. Lewis,* 473 A.2d 805 (Del. 1984), a case in which the Delaware Supreme Court had reversed (on discretionary interlocutory review) the Court of Chancery's denial of a motion to dismiss a derivative suit challenging a transaction with a 47% stockholder that had been approved by a majority disinterested and independent board, but not by the corporation's stockholders. The Supreme Court in *Aronson* held that, unless a stockholder plaintiff pleads particularized facts calling into question the board's ability to exercise properly its independent and disinterested business judgment in responding to a demand to institute suit, a board's refusal to sue is subject to business judgment review. After extended discussion of post-*Aronson* case law, the Court determined that *Aronson* applies only to the demand-excusal context and does not provide an independent basis for changing the substantive standard of review of controlling stockholder transactions.

After finding that the operative standard of review was entire fairness with possible burden shifting based on the audit committee's approval of the service agreements, the Court held that the complaint supported a reasonable inference that the agreements were not entirely fair. Among the factors that the Court found to raise such inference were: (i) Cohen's voting control despite having only a 5.5% equity stake; (ii) the long history of advisory service agreements between the Company and Cohen's affiliates; (iii) the amount and timing of the payments; (iv) the minimal resources of Madison Park; (v) the duplication between the services Madison Park provided and the capabilities of the Company management; (vi) the lack of similar service agreements at any of EZCORP's peer companies; (vii) the decision by two members of the audit committee to cancel the renewal of one agreement; and (viii) Cohen's retaliation against those board members.

The Court added that at the motion to dismiss stage, the involvement of the audit committee in the transactions does not defeat the fiduciary duty claim because a determination of whether an independent committee is "well-functioning" requires a "fact intensive inquiry."

The Court next turned to its analysis under Court of Chancery Rule 23.1. The Court found that reasonable doubt existed as to the ability of a majority of the directors to exercise independent and disinterested business judgment over a demand, and thus that

demand was excused. Notably, the Court found demand excused as to a retired board member whom Cohen brought out of retirement and reappointed after removing three directors in July 2014. While the Court acknowledged the general rule that a director's nomination or election by an interested party is, by itself, insufficient to raise a reasonable doubt about his independence, "it is not necessarily irrelevant." The Court found that this director's alleged "eagerness to be of use," combined with his participation as an audit committee member in approving some of the challenged agreements, could support the reasonable inference that "Cohen wanted to bring back a cooperative member of the placid antebellum regime."

Corwin v. KKR Financial Holdings LLC, 125 A.3d 304 (Del. 2015).

In *Corwin v. KKR Financial Holdings LLC,* 125 A.3d 304 (Del. 2015), the Delaware Supreme Court affirmed a ruling by the Court of Chancery granting the defendants' motions to dismiss a suit challenging the acquisition of KKR Financial Holdings LLC ("KFN") by KKR & Co. L.P. ("KKR"). The Court held that the business judgment rule is the appropriate standard in post-closing damages suits involving mergers that are not subject to the entire fairness standard and that have been approved by a fully informed, uncoerced majority of the disinterested stockholders, even where such approval is statutorily required.

In December 2013, KKR and KFN executed a stock-for-stock merger agreement, which was subject to approval by a majority of KFN shares held by persons other than KKR and its affiliates. The merger, which was priced at a premium of 35% to market, was approved in April 2013 by an independent board majority and by a majority of disinterested stockholders.

Following the merger, nine lawsuits challenging the merger were brought in the Court of Chancery and consolidated. The plaintiffs alleged that (i) the members of the KFN board breached their fiduciary duties by agreeing to the merger, and (ii) KKR breached its fiduciary duty as a controlling stockholder by causing KFN to enter into the merger agreement. The plaintiffs' control claims focused on the facts that a KKR affiliate managed the company's day-to-day operations and that KFN's primary business was financing KKR's leveraged buyout activities.

The Court of Chancery dismissed the complaint, finding that KKR, which owned only 1% of KFN's stock, was not a controlling stockholder. Additionally, the Court of Chancery held that the business judgment rule would apply to the merger because the merger was approved by a majority of the shares held by the disinterested, fully informed stockholders of KFN.

The Supreme Court, sitting *en banc,* unanimously affirmed the judgment of the Court of Chancery. With respect to the control issue, the Court found that the plaintiffs had not alleged sufficient facts to support the argument that KKR had effective control of the board and could therefore prevent KFN's board from exercising its own independent judgment in determining whether to approve the merger. To support this finding, the Court noted that KKR "owned less than 1% of the stock, had no right to appoint any directors, and had no contractual right to veto any board decision." Accordingly, the Court rejected the plaintiffs' control claims.

The Court further held that the business judgment standard of review would apply to the merger "because it was approved by a majority of the shares held by disinterested stockholders of KFN in a vote that was fully informed." The Court also declined to review the Court of Chancery's holding on the non-applicability of *Revlon,* finding that even if *Revlon* applied to the merger, the voluntary approval by an informed majority of disinterested stockholders was sufficient to support application of the business judgment rule. The Court stated that *Revlon* and *Unocal* were not designed to address post-closing claims for money damages, but rather to provide stockholders and the Court of Chancery the ability to address merger and acquisition decisions before closing.

In so holding, the Court agreed with the Court of Chancery's interpretation of *Gantler v. Stephens,* 965 A.2d 696 (Del. 2009). In *Gantler,* the Supreme Court stated that ratification is limited to circumstances where a fully informed stockholder vote approves director action that does not legally require stockholder approval in

order to become effective. Using this interpretation, plaintiffs argued that the merger should be subject to heightened scrutiny regardless of the statutorily required stockholder vote approving the merger. The Court rejected this argument, finding that *Gantler* was a narrow decision that focused on the meaning of the term "ratification," and was not meant to overturn Delaware's "long-standing body of case law" regarding the effect of fully informed stockholder approval.

The Supreme Court noted, however, that its holding applies only to fully informed and uncoerced votes of disinterested stockholders. Thus, the business judgment rule is not invoked if material facts regarding the merger are not disclosed to the voting stockholders.

In re Trados Shareholders Litigation, 73 A.3d 17 (Del. Ch. 2013).

In a 115-page post-trial opinion in *In re Trados Inc. Shareholder Litigation,* 73 A.3d 17 (Del. Ch. 2013), the Court of Chancery found entirely fair the decision to approve a merger in which common stockholders received no consideration.

In 2000, Trados Inc. ("Trados") obtained venture capital to support a growth strategy intended to lead to an initial public offering. The venture capital firms received preferred stock and placed representatives on the Trados board of directors.

In July 2005, Trados was acquired by SDL plc for $60 million in cash and stock. The preferred stockholders received $52.2 million of that amount in their liquidation preference, and management received $7.8 million as part of an existing management incentive plan. The common stockholders received no merger consideration. The plaintiff, a common stockholder, sought appraisal and sued the Trados directors for breach of fiduciary duties. In 2009, then-Chancellor Chandler denied in part a motion to dismiss, ruling that the plaintiff had sufficiently alleged that the venture firms' directors were interested in the decision to pursue the merger.

The Court reviewed the transaction for entire fairness and found that, although the process was not fair, the decision to approve the merger was entirely fair because the common stock had no economic value before the merger and its appraised value was zero. The Court also ordered the parties to enter into a schedule for briefing the issue of attorneys' fees.

Aiding & Abetting Liability

RBC Capital Markets, LLC v. Jervis, 2015 WL 7721882 (Del. Nov. 30, 2015).

In *RBC Capital Markets, LLC v. Jervis,* 2015 WL 7721882 (Del. Nov. 30, 2015), the Delaware Supreme Court affirmed a post-trial decision by the Court of Chancery holding that a financial advisor was liable for aiding and abetting breaches of fiduciary duty by directors of a corporation during a sale of control transaction. In doing so, the Court held that the evidence supported a finding that the advisor had the necessary scienter for an aiding and abetting claim; that is, the financial advisor "knowingly participated" in the breach by "exploiting its own conflicted interests to the detriment of [the corporation] and by creating an informational vacuum." The Court refused to require contribution from directors (who had previously settled with the stockholder-plaintiffs) because the board was exculpated from monetary liability under the Company's Section 102(b)(7) provision. The Court confirmed, however, that Section 102(b)(7) protections do not extend to third parties.

In December 2010, the board of Rural/Metro Corporation ("Rural" or the "Company") formed a special committee to explore strategic alternatives. While the special committee was authorized to hire a financial advisor to help explore these options, it was not expressly authorized to initiate a sale process. After interviewing two other financial advisors, the special committee engaged RBC Capital Markets ("RBC") as its primary financial advisor. In its presentation to the special committee, RBC had recommended a sale of the Company in a coordinated effort with the sale of Rural's competitor, Emergency Medical Services Corporation ("EMS"), because "healthcare was 'strong'" and selling the Company at that point in time was "opportunistic." But RBC "did not disclose that

proceeding in parallel with the EMS process served RBC's interest in gaining a role on the financing trees of bidders for EMS." RBC sought to use as an "angle" its role as a sell-side advisor to secure a buy-side financing role for the EMS deal, which could entitle RBC to "$60.1 million in fees from the Rural and EMS deals."

After contacting several private equity firms, six submitted indications of interest, and ultimately, Warburg Pincus LLC submitted the highest bid of $17.25 per share. RBC unsuccessfully solicited a "buy-side financing role from Warburg," but did not disclose its attempt to the special committee. RBC and Moelis & Company ("Moelis"), the special committee's secondary financial advisor, provided fairness opinions. The Court of Chancery found that "RBC worked to lower the analyses in its fairness presentation so Warburg's bid looked more attractive. Specifically, the trial court found that RBC made a series of changes to its fairness analysis" without disclosing these changes to the special committee. That analysis was sent to the board just three hours before its meeting to decide on the deal. The board approved the merger with Warburg in March 2011, and in June 2011, the merger closed, after approval by the Company's stockholders.

The class plaintiffs sought relief against Rural's directors for breaches of fiduciary duty and against RBC and Moelis for aiding and abetting those breaches. Rural's directors and Moelis settled, and RBC went to trial. Post-trial, the Vice Chancellor held that RBC was liable for aiding and abetting breaches of the directors' duty of care and duty of disclosure. Specifically, the trial court held that the board breached its duty of care under *Revlon*'s enhanced scrutiny standard after an unreasonable sales process, and that the board failed to disclose material information in its proxy statement regarding RBC's valuation process and conflicts. Concluding that RBC had knowingly aided and abetted these breaches, the Court of Chancery found RBC liable for $75.7 million. This represented 83% of the damages, which the Court determined was reasonable, given the Delaware Uniform Contribution Among Tortfeasors Act and RBC's responsibility as a joint tortfeasor.

The Delaware Supreme Court affirmed. First, after concluding that *Revlon* applied, the Court reviewed the trial court's holding that Rural's board breached its duty of care under enhanced scrutiny. The Court of Chancery had found that the board's pursuit of the transaction was outside the range of reasonableness, because "RBC did not disclose that proceeding in parallel with the EMS process served RBC's interest in gaining a role on the financing trees of bidders for EMS," and that these actions "impeded interested bidders from presenting potentially higher value alternatives." The board, according to the Court, should have been aware of the negative implications of this dual-track structure and should have had a mechanism to identify RBC's conflicts. "[D]irectors need to be active and reasonably informed when overseeing the sales process, including identifying and responding to actual or potential conflicts of interest," and "the board should require disclosure of, on an ongoing basis, material information that might impact the board's process" when there is a conflicted advisor.

The Court of Chancery also had found that Rural's board was not "adequately informed as to Rural's value," including that the "Company's value on a stand-alone basis exceeded what a private equity bidder willingly would pay." And because the directors were not "well-informed" as to the value, their decision was "devoid of important efforts" necessary to "to protect… stockholders and to ensure that the transaction was favorable to them." The "informational vacuum created by RBC" also made it impossible for stockholders to check the board and ensure that they had diligently contemplated the decision to sell the Company. This informational vacuum also contributed to the Court of Chancery's holding that Rural's board had violated its duty of disclosure by failing to disclose RBC's conflicts fully and characterize RBC's analysis accurately. The Supreme Court affirmed these rulings.

Next, the Court held that RBC had aided and abetted the board's breaches. The Court affirmed the trial court's "narrow holding" that "if [a] third party knows that the board is breaching its duty of care and participates in the breach by misleading the board or creating the informational vacuum, then the third party can be liable for aiding and abetting." Even though "the requirement that the aider and abettor act with scienter makes an aiding and abetting claim among the most

difficult to prove," the Court found that the requisite scienter had been shown because RBC "intentionally duped" the board into breaching its duty of care and engaged in "fraud on the Board" by knowingly creating the informational vacuum.

Finally, the Court rejected RBC's argument that it had a right to contribution from joint tortfeasors, noting that the settlement agreements barred such a right. Importantly, the Court also held that Rural's Section 102(b)(7) exculpatory provision did not shield RBC from liability. "While Section 102(b)(7) insulates directors from monetary damages stemming from a breach of the duty of care, its protection does not apply to third parties such as RBC." The intended legislative purpose of Section 102(b)(7) was not to "safeguard third parties and thereby create a perverse incentive system wherein trusted advisors to directors could, for their own selfish motives, intentionally mislead a board only to hide behind their victim's liability shield."

In re Rural Metro Corporation Stockholders Litigation, 88 A.3d 54 (Del. Ch. 2014); 102 A.3d 205 (Del. Ch. 2014).

In a 91-page post-trial opinion in *In re Rural Metro Corporation Stockholders Litigation,* 88 A.3d 54 (Del. Ch. 2014), the Delaware Court of Chancery held RBC Capital Markets, LLC ("RBC") liable for aiding and abetting breaches of fiduciary duty by the board of directors of Rural/Metro Corporation in connection with Rural's acquisition by Warburg Pincus LLC. The case proceeded against RBC even though Rural's directors, as well as Moelis & Company LLC, which had served as financial advisor in a secondary role, had settled before trial.

The Court found that RBC, in negotiating the transaction on behalf of Rural, had succumbed to multiple conflicts of interest. According to the Court, RBC, motivated by its contingent fee and its undisclosed desire and efforts to secure the lucrative buy-side financing work, prepared valuation materials for Rural's board that made Warburg's offer appear more favorable than it was. Because those valuation materials were included in Rural's proxy statement, the Court found that RBC was also liable for aiding and abetting the board's breach of its duty of disclosure.

Despite its finding of liability, the Court stated that it is not yet in a position to determine an appropriate remedy. The Court also deferred ruling on the plaintiffs' request for fee shifting, but it noted that, "given the magnitude of the conflict between RBC's claims and the evidence, it seems possible that the facts could support a bad faith fee award."

In an opinion assessing damages in *In re Rural/Metro Corp. S'holders Litig.,* 102 A.3d 205 (Del. Ch. 2014), the Court of Chancery held that RBC, which had been held liable in the earlier opinion for aiding and abetting breaches of fiduciary duty by a board of directors in connection with approving a merger and related disclosures, would be required to pay 83% of the damages to the stockholder class. Relying on a discounted cash flow analysis, the Court determined that the fair value of Rural/Metro on a quasi-appraisal basis fell short of the merger price by $4.17 per share, and that the damages to the class of stockholders not affiliated with the defendants totaled approximately $91.3 million.

Rural/Metro, its directors and the company's other financial advisor had settled before trial and obtained "joint tortfeasor" releases, under which the plaintiff class agreed that the damages recoverable against other tortfeasors would be reduced to the extent of the settling defendants' respective pro rata shares, as permitted by the Delaware Uniform Contribution Among Tortfeasors Law. The Court held that the unclean hands doctrine barred the non-settling financial advisor from claiming a settlement credit as to claims involving that financial advisor's adjudicated "fraud upon the board," but that it could claim a settlement credit as to other claims. The Court determined that the record at trial supported a finding that two of Rural/Metro's directors were joint tortfeasors, but did not support such a finding as to the other directors or the settling financial advisor. Allocating responsibility for the various claims on which liability had been previously found, the Court entered judgment for approximately $75.8 million against RBC.

Deal Protection Devices

In re Comverge, Inc. Shareholders Litigation, 2014 WL 6686570 (Del. Ch. Nov. 25, 2014).

In *In re Comverge, Inc. Shareholders Litigation,* 2014 WL 6686570 (Del. Ch. Nov. 25, 2014), the Delaware Court of Chancery granted in part the defendants' motion to dismiss a post-closing stockholder challenge to the acquisition of Comverge, Inc. ("Comverge") by H.I.G. Capital, L.L.C. ("HIG"), which acquisition the Court had previously declined to enjoin. The plaintiffs alleged that Comverge's board of directors breached its fiduciary duties by: (i) failing to bring suit against HIG for an alleged breach of a non-disclosure agreement ("NDA") between the parties; (ii) conducting a flawed sale process that failed to maximize value for Comverge's stockholders; and (iii) agreeing to preclusive deal protection measures that prevented Comverge from soliciting alternative bidders. The plaintiffs also claimed that HIG had aided and abetted the board in breaching its fiduciary duties.

Comverge had lost money every year of its existence and had long sought, to no avail, to solve its liquidity problems through various types of transactions. In November 2011, HIG contacted Comverge to express an interest in acquiring the company. In February 2012, the board declined HIG's offer to buy the company for $2.25 per share, in part because another bidder had suggested interest in a transaction with Comverge at a higher price. An affiliate of HIG thereafter acquired certain notes issued by Comverge, which allegedly violated the two-year standstill provision of the NDA. Following notification of HIG's actions, the board considered, but ultimately decided against, suing HIG for breach of the NDA. The notes gave HIG significant leverage over Comverge because they carried the right to accelerate Comverge's debt and provided HIG with prior approval rights over any acquisition transaction. HIG promptly took advantage of its leverage by notifying Comverge that it was in default under the notes and indicating that it would accelerate the debt under the notes unless the board accepted HIG's new, lower-priced offer to acquire the company for $1.50 per share. After further negotiation with HIG, the board agreed to a merger with HIG at a price of $1.75 per share. At the time of the board's approval of the merger, Comverge's stock was trading at $1.88 per share. The merger agreement included a go-shop period during which HIG agreed not to exercise its blocking rights under the notes. During the go-shop period, Comverge had the right to terminate the transaction to pursue a superior proposal by paying HIG a total fee of 5.55% of the deal's equity value. After the go-shop period, the total payment required to terminate the agreement rose to 7% of the deal's equity value. In addition, Comverge entered into a $12 million bridge financing agreement with HIG pursuant to which Comverge issued HIG notes that were convertible at HIG's election into shares of Comverge common stock at a conversion price of $1.40 per share, which was $0.35 lower than the deal price and $0.48 lower than the then-current trading price of Comverge's shares.

The Court granted the defendants' motion to dismiss in part, finding that the board's decision not to sue on the NDA and the board's sale process did not violate the board's fiduciary duties. The Court held that the board's decision to pursue a sale transaction rather than uncertain, costly and potentially time-consuming litigation against HIG based on a possible violation of the NDA was reasonable, especially in light of Comverge's dire financial situation. With respect to the plaintiffs' sale process claims, the Court found that the board had engaged in "hard-fought" negotiations with HIG, and had canvassed the market and considered alternatives to the transaction over an 18-month period before agreeing to the merger. While the sale process ultimately resulted in a lower deal price than HIG's initial offer, due to HIG's superior bargaining position after acquiring the notes, the Court found that the board's conduct at most amounted to a breach of the duty of care and did not support a claim for a non-exculpated breach of the duty of loyalty.

The Court also dismissed the aiding and abetting claims against HIG. The Court noted that Delaware case law recognizes an aiding and abetting claim if the acquirer in a merger induces the target board to breach its fiduciary duties "by extracting terms which require the opposite party to prefer its interests at the expense of the shareholders." While recognizing that HIG's

"hard-nosed and aggressive" negotiating strategy was designed to take advantage of Comverge's precarious financial position, the Court concluded that HIG had not exploited self-interest on the part of the members of the board in a manner that would give rise to liability for aiding and abetting a breach of fiduciary duty.

Finally, the Court found that it was conceivable that the combined effect of the termination fee, the expense reimbursement and the convertible bridge loan could have had an impermissibly preclusive effect on potential alternative bidders. The Court noted that, even at the lower end, the combined termination fee and potential expense reimbursement would be 5.55% of the equity value of the transaction and would test the limits of what the Court had found to be within a reasonable range for termination fees in its past decisions. At the higher end, the Court noted that the plaintiffs had contended that the combined fees and Comverge stock issuable under the notes upon termination of the merger agreement could amount to as much as 11.6% to 13.1% of the equity value of the transaction. In light of the potential magnitude of the combined fees and in the context of a deal with a negative premium to market, the Court held that it was reasonably conceivable that the board had acted unreasonably in adopting the potentially preclusive deal protection measures and refused to grant the defendants' motion to dismiss in respect of the plaintiffs' claim that the board breached its fiduciary duties in agreeing to such measures.

Disclosures

In re Trulia, Inc. Stockholder Litigation, 2016 WL 325008 (Del. Ch. Jan. 22, 2016).

In *In re Trulia, Inc. Stockholder Litigation,* 2016 WL 325008 (Del. Ch. Jan. 22, 2016), the Delaware Court of Chancery refused to approve a class action settlement that called for marginal disclosures in exchange for a broad release of stockholder claims. In so doing, the Court announced that moving forward it would review such "disclosure settlements" with increased scrutiny.

The case arose from the stock-for-stock merger between online real estate companies Zillow, Inc. and Trulia, Inc. Shortly after the merger was announced in July 2014, four plaintiffs filed class action complaints seeking to enjoin the merger and alleging that the directors of Trulia breached their fiduciary duties by including misleading disclosures in the joint proxy statement. Within days, however, the plaintiffs agreed to release their claims if Trulia would provide supplemental disclosures about the financial opinion the Trulia directors relied upon when approving the transaction. Trulia provided the disclosures, and the stockholders of both companies subsequently adopted the merger agreement. A formal settlement agreement was then submitted to the Court for approval, which (i) sought certification of a class consisting of all Trulia stockholders as of the date the merger was first announced through the closing date; (ii) included a broad release of "any claims arising under federal, state, statutory, regulatory, common law, or other law or rule" held by members of the proposed class relating in any way to the merger (with a limited carve-out for antitrust claims); and (iii) permitted plaintiffs' counsel to seek an award of attorneys' fees totaling $375,000.

The Court rejected the proposed settlement because the supplemental disclosures failed to provide a material benefit to the Trulia stockholders and were insufficient to justify the broad release of claims. In reaching this decision, the Court held that certain disclosures were immaterial because they contained information that was already publicly available, while other disclosures, which restated specific data points used by Trulia's financial advisor, were immaterial because Delaware law only requires companies to provide a summary of the financial advisor's opinion and not every detail necessary to recalculate the advisor's analysis.

In addition to its ruling, the Court unambiguously announced its intention to review "disclosure settlements" in the future with heightened scrutiny. The Court acknowledged that defendants involved in deal litigation have strong incentives to settle quickly—particularly if such settlements can be obtained by offering minimal disclosures in exchange for a broad release of stockholder claims. The Court explained,

however, that its prior willingness to approve settlements calling for marginal disclosures, sweeping releases of stockholder claims and six-figure attorney fees had led to an explosion of lawsuits that "serve[] no useful purpose." Stressing how it can be problematic to adjudicate disclosure claims in the context of settlement-approval proceedings, the Court further explained that such proceedings are non-adversarial, leaving the Court to determine the materiality of supplemental disclosures without the benefit of a full record or consulting opposing briefs. Given the surge in deal litigation and the risk that stockholders are losing potentially valuable claims that have not been adequately investigated, the Court proposed two solutions.

First, the Court recommended that disclosure claims be litigated outside of a settlement-approval proceeding and in an adversarial context. One such context would be a preliminary injunction motion, where plaintiffs would bear the burden of showing that disclosure of the omitted fact would likely have been material to a reasonable investor. Another context is when plaintiffs' counsel apply to the Court for an award of attorneys' fees after defendants voluntarily decide to supplement their proxy materials by making one or more of the disclosures sought by plaintiffs, thereby mooting some or all of their claims. In this situation, defendants are incentivized to oppose excessive fee requests.

Second, to the extent parties continue to pursue disclosure-based settlements, the Court warned that such settlements are "likely to be met with continued disfavor" by the Court unless the supplemental disclosures address a "plainly material misrepresentation or omission," and the subject matter of the proposed release is narrowly circumscribed to encompass nothing more than disclosure claims and fiduciary duty claims concerning the sale process.

Should supplemental information not be "plainly material," the Court recommended appointing an *amicus curiae,* paid for by both parties, to assist the Court in evaluating the alleged benefits of the supplemental disclosures. Finally, to mitigate the risk that parties will seek out forums willing to approve disclosure settlements of no genuine value, the Court also called on its sister courts in other states to adopt similar practices.

Following the settlement hearing, the Court noted that the parties agreed to narrow the release to exclude unknown claims, foreign claims, and claims arising under state or federal antitrust law. However, the Court held that this narrowed release was still overbroad as it was not limited to solely disclosure claims and fiduciary duty claims concerning the decision to enter into the merger.

Merger Agreement Construction

Cigna Health & Life Insurance Company v. Audax Health Solutions, Inc., 107 A.3d 1082 (Del. Ch. 2014).

In *Cigna Health & Life Insurance Company v. Audax Health Solutions, Inc.,* 107 A.3d 1082 (Del. Ch. 2014), the Delaware Court of Chancery found invalid features of a private company merger agreement that required stockholders, as a condition to receiving their merger consideration, to submit a letter of transmittal agreeing to provide a release of all claims against the acquirer and that further required stockholders to indemnify, for an indefinite period of time, the acquirer for claims arising from the seller's breach of representations and warranties.

The opinion arose from the acquisition of Audax Health Solutions, Inc. ("Audax") by Optum Services, Inc. ("Optum"). In connection with the merger, certain stockholders of Audax executed support agreements that included: (i) a release of all claims against Optum and its affiliates; (ii) an agreement to be bound by the terms of the merger agreement, specifically including the provisions indemnifying Optum and its affiliates for any breaches of the representations and warranties; and (iii) an appointment of a stockholder representative. In order to receive the merger consideration under the merger agreement, stockholders who did not execute the support agreements were required to execute the letter of transmittal containing the release. Following the merger, Cigna Health and Life Insurance Company ("Cigna"), a holder of preferred stock of Audax who did not execute a support agreement and refused to execute the letter of transmittal, challenged, among

other things, the validity of the release in the letter of transmittal and the indemnification provisions of the merger agreement.

On Cigna's motion for judgment on the pleadings, the Court held that the purported release in the letter of transmittal was unenforceable due to a lack of consideration. In so holding, the Court rejected the defendants' argument that the release was integral to the overall transaction, noting that provisions in the merger agreement that required the letter of transmittal to be in form and substance reasonably acceptable to the acquirer did not indicate that the stockholders would be required to agree to the release. The Court further explained that endorsing the defendants' position would permit buyers to force post-closing conditions or obligations not referenced in the merger agreement on the stockholders in a letter of transmittal. Accordingly, the Court found that the release constituted a new obligation that was unenforceable absent consideration. The Court held that the merger consideration could not constitute consideration for the release because the stockholders had already become entitled to it by operation of law upon the closing of the merger.

The Court also held that the indemnification provisions were unenforceable against stockholders who had not executed the support agreements. In response to Cigna's challenges to the indemnification provisions, the defendants argued that the indemnification obligation was substantively no different from an escrow arrangement, which is common in private company mergers and has previously been recognized by the Delaware courts as enforceable. Despite noting the economic similarities between the indemnification provisions and an escrow arrangement, the Court found that "the merger consideration here more aptly can be described as cash, subject to an open-ended post-closing price adjustment." In this connection, the Court explained that such price adjustments are permissible under Delaware law if they comply with Section 251 of the General Corporation Law of the State of Delaware (the "DGCL"), which requires a merger agreement to set forth a determinable merger consideration by stating the cash, property, rights or securities that the stockholders are entitled to receive in the merger.

In determining whether the indemnification provisions violated Section 251 of the DGCL, the Court distinguished the facts at hand from those in *Aveta, Inc. v. Cavallieri,* 23 A.3d 157 (Del. Ch. 2010). In *Aveta*, the Court of Chancery found that the post-closing price-adjustment procedures in a merger agreement (which included an earn-out, adjustments based on the company's financial statements, and a potential claw-back) were permissible under Section 251 of the DGCL. The Court noted that, unlike the merger agreement in *Aveta,* the indemnification provisions in the Audax-Optum merger agreement were not limited in terms of the amount of money that might be subject to a claw-back or the time period during which Optum could potentially bring a claim for indemnification. Rather, the indemnification structure in the Audax-Optum merger agreement continued indefinitely and made the value of the merger consideration indeterminable. Accordingly, the Court held that the merger agreement failed to set forth the value of the merger consideration as required by Section 251 of the DGCL because of the open-ended and unlimited indemnification provisions. The Court further held that the indemnification provisions were unenforceable against stockholders who did not specifically agree to such obligations by executing the support agreements or the merger agreement itself.

The Court specifically noted the narrow scope of the opinion and clarified that it was not deciding issues relating to (i) escrow agreements generally, (ii) the general validity of post-closing price adjustments requiring direct repayment from stockholders, (iii) whether a time-limited price adjustment that covers all of the merger consideration may be valid, or (iv) whether an indefinite adjustment period as to a portion of the merger consideration may be valid. Instead, the Court explained that it was the combination of the indefinite and contingent nature of the entirety of the consideration payable under the Audax-Optum merger agreement that resulted in the violation of Section 251 of the DGCL.

Cooper Tire & Rubber Company v. Apollo (Mauritius) Holdings Pvt. Ltd, 2014 WL 5654305 (Del. Ch. Oct. 31, 2014).

In *Cooper Tire & Rubber Company v. Apollo (Mauritius) Holdings Pvt. Ltd,* 2014 WL 5654305 (Del. Ch. Oct. 31,

2014), the Delaware Court of Chancery found that Cooper Tire & Rubber Company ("Cooper") had not satisfied all of the conditions to closing its merger with Apollo (Mauritius) Holdings Pvt. Ltd ("Apollo") as of the trial date, and thus was likely barred from seeking a $112 million reverse termination fee under the merger agreement.

Cooper and Apollo entered into a merger agreement pursuant to which Apollo would acquire Cooper. Shortly thereafter, a series of events occurred that precipitated the deal's demise. First, a labor union at Chengshan Cooper Tires ("CCT"), a Chinese facility that was majority owned by Cooper, publicly stated its opposition to the merger and commenced an employee strike in protest. The union also physically barred Cooper-appointed managers from entering the facility or obtaining access to CCT's financial data entry systems. It was alleged that the parties later determined that the CCT strike had been initiated by Cooper's minority partner at CCT, who opposed the merger. At the same time, Cooper encountered resistance from its domestic union, the United Steel Workers ("USW"), which claimed that the merger triggered Cooper's obligations to renegotiate its collective bargaining agreements. Apollo attempted to negotiate with the USW, but was unsuccessful in resolving the dispute.

Once it became clear that the deal was in danger of failing, Cooper sued Apollo in the Court of Chancery seeking specific performance or damages for breach of contract based on Apollo's alleged failure to negotiate with the USW in good faith. The Court of Chancery, in an earlier opinion, *Cooper Tire & Rubber Company v. Apollo (Mauritius) Holdings Pvt. Ltd,* 2013 WL 5977140 (Del. Ch. Nov. 9, 2013), ruled against Cooper, which then sought interlocutory appeal of the Court's decision to the Delaware Supreme Court. While the appeal was pending, Cooper notified the Delaware Supreme Court that it intended to terminate the merger agreement and seek a reverse termination fee under the merger agreement rather than pursue its appeal. Apollo then sought to prevent Cooper from collecting the reverse termination fee by seeking a declaratory judgment from the Court that Cooper had not satisfied all conditions to closing the merger. Specifically, Apollo alleged that Cooper was, at the time of trial, in breach of its obligation under the merger agreement to cause each of its subsidiaries to operate in the ordinary course of business. Cooper argued that the interim covenant only applied to actions within Cooper's complete control and that the alleged breaches involved third parties, such as CCT's employees and the USW, that were outside the scope of the interim covenant.

The Court rejected Cooper's interpretation of the interim covenant and held that the events that had occurred at the CCT facility prevented Cooper from complying with its contractual obligations necessary to close the merger. The Court stated that "ordinary course" means "the normal and ordinary routine of conducting business," and that the cessation of CCT's production of Cooper-branded tires, the physical exclusion of Cooper employees from CCT's facilities, and limitation of Cooper's access to CCT's financials did not comply with that standard. While stating that its opinion only addressed whether Cooper had satisfied its obligations under the merger agreement and the conditions to closing, the Court noted that the effect of the opinion likely would be dispositive of Cooper's ability to collect a reverse termination fee.

Great Hill Equity Partners IV, LP v. SIG Growth Equity Fund I, LLLP, 80 A.3d 155 (Del. Ch. 2013); 2014 WL 6703980 (Del. Ch. Nov. 26, 2014).

In *Great Hill Equity Partners IV, LP v. SIG Growth Equity Fund I, LLLP,* 80 A.3d 155 (Del. Ch. Nov. 15, 2013), the Court of Chancery interpreted Section 259 of the General Corporation Law of the State of Delaware to hold that all privileges—including the attorney-client privilege—pass in a merger from the acquired corporation to the surviving corporation. Specifically, the Court held that, without a contractual provision to the contrary, even the seller's pre-merger attorney-client communications with respect to the merger itself would pass to the surviving corporation. The Court suggested that parties concerned about this issue should "use their contractual freedom in the manner shown in prior deals to exclude from the transferred assets the attorney-client communications they wish to retain as their own."

In a fact-intensive, 76-page motion to dismiss opinion, *Great Hill Equity Partners IV, LP v. SIG Growth Equity Fund I, LLLP,* 2014 WL 6703980 (Del. Ch. Nov. 26, 2014), the Delaware Court of Chancery largely denied the defendants' motions to dismiss fraud claims arising out of the sale of Plimus, a private Delaware corporation (the "Company"), to Great Hill, a private equity fund. The Court analyzed the specific factual allegations of a complaint that had been amended following the Court's earlier opinion holding that the Company's privileges, including pre-sale communications with counsel, passed to Great Hill in the merger by which it acquired the Company. *See Great Hill Equity Partners IV, LP v. SIG Growth Equity Fund I, LLLP,* 80 A.3d 155 (Del. Ch. 2013). The Court found that the amended complaint stated a claim for civil conspiracy and aiding and abetting fraud against a private equity fund that before the sale was the Company's single largest stockholder and had two designees on the Company's five-person board of directors. The Court also held that the amended complaint stated a claim for fraud against the selling private equity fund's two director designees.

The *Great Hill* opinion provides significant insight into issues arising in connection with private company M&A transactions, applying well-established law in the context of detailed factual allegations of fraud.

Implied Covenant of Good Faith & Fair Dealing

Lazard Technology P'rs, LLC v. QinetiQ North America Operations LLC, 114 A.3d 193 (Del. Apr. 23, 2015).

In *Lazard Technology P'rs, LLC v. QinetiQ North America Operations LLC,* 114 A.3d 193 (Del. Apr. 23, 2015), the Delaware Supreme Court affirmed the Court of Chancery's post-trial bench ruling and held that the defendant-below did not breach an earn-out provision in a merger agreement or the implied covenant of good faith and fair dealing.

In 2009, QinetiQ North America Operations, LLC (the "buyer"), a defense and security technology company, acquired Cyveillance, Inc. (the "company"), a cyber-technology company. The buyer paid $40 million for the company up front and was obligated to make additional earn-out payments of up to $40 million if the company achieved certain revenue targets over a defined period. Section 5.4 of the merger agreement prohibited the buyer, post-closing, from "tak[ing] any action to divert or defer [revenue] with the intent of reducing or limiting the Earn-Out Payment." At the close of the earn-out period, revenues had not reached the level required to generate an earn-out.

Lazard Technology Partners, LLC, which represented former stockholders of the company (collectively, the "seller"), filed suit in the Court of Chancery on August 29, 2011 against the buyer. The seller alleged that the buyer breached both Section 5.4 of the merger agreement and the implied covenant of good faith and fair dealing by failing to take actions to achieve revenue sufficient to generate an earn-out. In a bench ruling following post-trial argument, the Court of Chancery entered judgment in favor of the buyer on both claims. With respect to the breach of contract claim, the Court concluded that the literal terms of Section 5.4 required a showing of intent, which the seller could not establish. The Court construed the implied covenant of good faith and fair dealing to prohibit only conduct undertaken with intent to reduce or avoid an earn-out payment altogether, consistent with the language of Section 5.4.

The Delaware Supreme Court affirmed. The Court agreed that Section 5.4 employed an intent standard, not a knowledge standard, and rejected the seller's assertion that the contract precluded conduct by the buyer that the buyer knew would compromise the seller's ability to receive an earn-out payment. On the implied covenant claim, the Court noted both the specific standard in Section 5.4 and the negotiating history (in which the seller had sought tighter objective controls on the buyer's post-closing conduct, but had failed to obtain them), stated that the Court of Chancery "was very generous in assuming that the implied covenant of good faith and fair dealing operated at all as to decisions affecting the earn-out," and held that

the Court of Chancery had correctly concluded that the implied covenant "did not inhibit the buyer's conduct unless the buyer acted with the intent to deprive the seller of an earn-out payment."

Orckit Communications Ltd. v. Networks³ Inc., C.A. No. 9658-VCG (Del. Ch. Jan. 28, 2015) (TRANSCRIPT).

In *Orckit Communications Ltd. v. Networks³ Inc. et al.*, C.A. No. 9658-VCG (Del. Ch. Jan. 28, 2015) (TRANSCRIPT), the Delaware Court of Chancery granted defendant Networks³'s motion to dismiss a claim that it had wrongfully terminated an agreement to purchase patents from plaintiff Orckit. The purchase of the patents was contingent upon the issuance of an approval by an Israeli government agency, and the agreement provided that "the terms in the…Approval shall be satisfactory in the sole discretion (which for purposes of this condition shall not, to the extent permitted by law, be subject to the implied covenant of good faith and fair dealing) of Networks³." The Court held that, under the agreement, whether the terms of the approval were satisfactory to Networks³ was "a decision that is unreviewable in the sense that, if it is timely taken, the defendant could then…terminate."

Orckit had alleged that, under the agreement, Networks³'s exercise of its sole discretion was qualified by either (i) a "commercially reasonable efforts" standard appearing elsewhere in the contract, or (ii) a default good faith standard that could not be disclaimed, and that, under either standard, Networks³ had breached the agreement. The Court rejected both arguments. In regard to the first, the Court found it unreasonable to assume that the parties would expressly disclaim the application of the implied covenant of good faith and fair dealing only to impose a higher standard. Further, the Court held that basic "canons of construction" provided that a specific discretionary standard in a particular provision controls over a general one elsewhere in a contract. In regard to the second, the Court, emphasizing that "Delaware is a contractarian state" and that "the language that the parties have agreed to…governs the enforcement of contracts," stated that the provision's "language…could not be any clearer," and that it was, in fact, "as clear as it gets." ■

Stockholder Rights Plans

Third Point LLC v. Ruprecht, et al., 2014 WL 1922029 (Del. Ch. May 2, 2014).

In *Third Point LLC v. Ruprecht, et al.,* 2014 WL 1922029 (Del. Ch. May 2, 2014), the Delaware Court of Chancery denied preliminary injunctive relief against Sotheby's annual meeting, scheduled for May 6, 2014. The plaintiffs, including Third Point LLC and other stockholders, claimed that the board had violated its fiduciary duties by (i) adopting a stockholder rights plan with a two-tiered trigger, capping stockholders who file Schedule 13Ds at 10% of the outstanding stock, but permitting passive investors who file Schedule 13Gs to acquire up to 20% of the outstanding stock; and (ii) refusing to grant Third Point, the company's largest stockholder, a waiver enabling it to acquire up to 20% of the outstanding stock. Claiming that the board had acted for the primary purpose of inhibiting Third Point's ability to wage a successful proxy contest, Third Point asked the Court to apply the *Blasius* standard, and argued alternatively that the board's actions were impermissible under the *Unocal* standard. The board argued, among other things, that Third Point's accumulation of Sotheby's stock posed a legally cognizable threat to Sotheby's and that the board's actions in response were proportionate to the threat.

The Court held on a preliminary basis that *Unocal,* rather than *Blasius,* provides the appropriate framework of analysis. Applying the *Unocal* standard, the Court held on a preliminary basis that the majority-independent board had shown that it acted reasonably in identifying a legally cognizable threat—that Third Point, alone or with others, might acquire a controlling interest in the company without paying Sotheby's other stockholders a premium—and that its response to the threat was reasonable. The Court wrote that the issue of the board's refusal of Third Point's request for a waiver presented "a much closer question" than the original adoption of the rights plan, but determined that the board made a sufficient showing as to the threat that Third Point might be able to exercise "negative control" if permitted to accumulate up to 20% of the outstanding stock. Accordingly, the Court denied the application for preliminary injunction.

On May 5, 2014, Sotheby's and Third Point announced a resolution of the dispute, under which Third Point will be allowed to increase its ownership to 15% of the outstanding stock, the board will expand from twelve members to fifteen, and Third Point's three nominees will be appointed to the board and added to the company's slate of nominees at the 2014 annual meeting, which will be convened and adjourned to allow updated solicitation materials to be distributed.

Appraisal Actions & Proceedings

Merlin Partners LP v. AutoInfo, Inc., 2015 WL 2069417 (Del. Ch. Apr. 30, 2015); ***In re LongPath Capital, LLC v. Ramtron International Corporation,*** 2015 WL 4540443 (Del. Ch. June 30, 2015).

In two recent post-trial opinions in appraisal cases under 8 *Del. C.* § 262, the Court of Chancery addressed the importance of merger price and process as well as the reliability of discounted cash flow (DCF) analyses in determining fair value. In *Merlin Partners LP v. AutoInfo, Inc.,* 2015 WL 2069417 (Del. Ch. Apr. 30, 2015), Vice Chancellor Noble found that, where there was an adequate sale and negotiation process conducted at arm's length and there were no reliable cash flow projections from which to make a DCF analysis nor available alternate valuations, the price received in the merger, $1.05 per share, was the best indication of fair value at the time of the merger. Two months later, in *In re LongPath Capital, LLC v. Ramtron International Corporation,* 2015 WL 4540443 (Del. Ch. June 30, 2015), Vice Chancellor Parsons similarly determined that there were no reliable means of appraisal valuation other than the merger price, but also found that the fair value at the time of the merger was $0.03 below the deal price of $3.10 per share after accounting for synergies.

Under Section 262, stockholders who choose not to participate in certain merger transactions may petition the Court to determine the fair value of their stock. "Fair value" represents "the value to a stockholder of the firm as a going concern, as opposed to the firm's value in the context of an acquisition or other transaction." To determine fair value, the Court independently evaluates the evidence and may consider techniques or methods that are generally considered acceptable in the financial community and otherwise admissible in court. Depending on the case, the Court may rely upon a DCF analysis, a comparable transactions analysis, a comparable companies analysis, or the merger price itself. Delaware courts tend to favor a DCF model over other available methodologies in an appraisal proceeding. However, a DCF analysis has "much less utility" in cases where the transaction was an arm's-length merger or where the data inputs used in the model are not reliable.

After struggling financially, AutoInfo began a sale process. As part of the process, Stephens Inc., AutoInfo's financial advisor retained to assist with the sale process, asked management to prepare five-year financial projections that were "aggressively optimistic" for use in marketing AutoInfo. AutoInfo's management had never prepared multi-year projections before, and the company's CEO described the process as "a bit of a chuckle and a joke." Despite this, AutoInfo engaged in an extensive sales process, with Stephens contacting 164 potential strategic and financial buyers, 70 of which entered into non-disclosure agreements. Several bidders submitted letters of intent, including Comvest, which signed a letter of intent at $1.26 per share but eventually reduced its price to $1.05 per share after discovering problems with the reliability of AutoInfo's financial information.

Merlin Partners filed an appraisal action and, relying on two comparable companies analyses and a DCF analysis prepared by its financial expert, argued that the fair value of the company was $2.60 per share. The Court first found that Merlin's DCF analysis deserved little deference because Merlin had failed to establish the credibility of the management projections upon which it relied. Not only were they AutoInfo's first attempt at such projections, they had also been specifically prepared to "paint the most optimistic and bright current and future condition of the company" possible in connection with the sales process. The Court also gave no weight to Merlin's comparable companies analyses because the companies used for comparison differed significantly in size from AutoInfo (from more than twice to 300 times its size) and also used store-based business models rather than AutoInfo's riskier agent-based model. Conversely, AutoInfo's expert relied on merger price, and the Court found that it could place "heavy weight" on a merger price in the absence of any other reliable valuation analysis. Finding that fair value was the deal price, the Court noted that the merger was the result of a competitive and fair auction because AutoInfo: (i) retained an investment bank experienced in the transportation industry using an incentive-based fee structure; (ii) contacted numerous companies in the sales process; (iii) formed a special committee; (iv) was sold at a premium to market; and (v) had no other topping bid emerge between announcement and closing of the merger.

In *Ramtron,* after rejecting Cypress Semiconductor Corporation's bear hug letter to acquire all of its shares, as well as engaging in a subsequent sales process that involved its advisor contacting twenty-four potential buyers and executing non-disclosure agreements with six of those potential buyers, Ramtron engaged in negotiations with Cypress. After rejecting two more offers from Cypress, Ramtron agreed with Cypress on a final transaction price of $3.10 per share. LongPath, which acquired its shares after announcement of the merger, demanded appraisal and argued that fair value was $4.96 per share. The Court determined that LongPath's DCF analysis was not appropriate because it relied on management projections prepared by newer employees who were creating multi-year projections for the first time, which also utilized a point-of-sale revenue recognition methodology rather than Ramtron's historic point-of-purchase method. As further evidence of the unreliability of the projections, the Court noted that they were created after Cypress's bear hug letter, in anticipation of potential litigation or a hostile takeover bid, and that Ramtron, which already had a questionable track record at forecasting, prepared separate projections to provide to its bank. The Court also afforded no weight to LongPath's comparable

transactions analysis, as the petitioner's expert had a "dearth of data points" and could only point to two comparable transactions with vastly different multiples. Instead, the Court found it could give "one-hundred percent weight" to merger price as evidence of fair value when the merger resulted from a proper process. Here, only one company, Cypress, ever made a bid even after an active solicitation process, and Ramtron could and did repeatedly (and publicly) reject Cypress's overtures, after which Cypress raised its price. In addition, the Court determined that it was appropriate to subtract LongPath's estimate of net synergies of $0.03 per share (which was reached by netting negative revenue synergies and transaction costs from Ramtron's estimate of positive synergies) from the merger price to reach a fair value determination of $3.07 per share.

As these decisions illustrate, even though Delaware courts "tend to favor a DCF model in appraisal proceedings," they will be willing to rely entirely upon or afford substantial weight to the merger price to determine fair value where there is reason to question the reliability of the underlying management projections and where no other viable alternate valuation technique exists.

Merion Capital LP v. BMC Software, Inc., 2015 WL 67586 (Del. Ch. Jan. 5, 2015); ***In re Appraisal of Ancestry.com, Inc.,*** 2015 WL 66825 (Del. Ch. Jan. 5, 2015).

In two opinions issued the same day, the Delaware Court of Chancery addressed standing requirements under Delaware's appraisal statute, Section 262 of the General Corporation Law of the State of Delaware. In both *Merion Capital LP v. BMC Software, Inc.,* 2015 WL 67586 (Del. Ch. Jan. 5, 2015), and *In re Appraisal of Ancestry.com, Inc.,* 2015 WL 66825 (Del. Ch. Jan. 5, 2015), the Court found that a 2007 amendment to the appraisal statute did not impose a "share-tracing" requirement on an appraisal petitioner's right to demand appraisal of shares acquired after the record date for determining the stockholders entitled to vote on a merger. In so doing, the Court rejected a potential obstacle to so-called "appraisal arbitrageurs" that seek to use Delaware's appraisal process to capitalize on potentially undervalued transactions by purchasing shares of the target company's stock after announcement of a merger.

In *BMC Software,* petitioner Merion Capital LP ("Merion") sought appraisal for 7.6 million shares of common stock of BMC Software, Inc. ("BMC") that were purchased after the record date for a going-private merger. Merion, the beneficial owner of the shares, requested its broker to direct the nominee record holder of its shares to demand appraisal with respect to the purchased shares on Merion's behalf, but the broker refused. Merion then transferred record ownership of the shares into its own name and delivered a formal demand for appraisal to the company. BMC argued that, in order to have standing to pursue its appraisal claims, Merion had the burden of showing that each share it acquired after the record date had not been voted in favor of the merger by the previous holders. The Court rejected this contention and held instead that the unambiguous language of the appraisal statute required Merion to show only that the record holder of the shares that made the demand (in this case, Merion itself) had not voted the shares in favor of the merger.

In *Ancestry.com,* Merion sought appraisal for 1,255,000 shares of common stock of Ancestry.com, Inc. ("Ancestry") purchased after the record date for a cash-out merger. Unlike in *BMC Software,* Merion never transferred its shares into record name, but instead directed Cede & Co., the nominee record holder of the shares, to demand appraisal on Merion's behalf. As permitted by a 2007 amendment to the appraisal statute, Merion, in its capacity as the beneficial owner of the shares, filed a petition for appraisal in the Court of Chancery. Ancestry.com argued that since Merion, as the beneficial owner of the shares, filed the petition for appraisal, Merion was required to show that it (rather than the record holder, Cede & Co.) did not vote the shares in favor of the merger. Moreover, Ancestry.com argued that because Merion acquired beneficial ownership of its shares after the record date, Merion was also required to show that its predecessor beneficial owners did not vote in favor of the merger. The Court rejected this argument as well, holding that an appraisal petitioner is only required to show that the record holder held of record at least as many shares not voted

in favor of the merger as the number for which appraisal demands were submitted.

In both *BMC Software* and *Ancestry.com*, the Court identified, but declined to address, the potential for a theoretical "over-appraisal" scenario, in which a record holder (such as Cede & Co.) would hold shares as nominee for many beneficial owners, would follow those beneficial owners' voting instructions, and would end up owning of record fewer shares not voted in favor of the merger than the number of shares as to which the record holder demanded appraisal. The Court noted that such a theoretical problem at most threatened the policy goals of the appraisal statute, but did not render the statute absurd or inoperable.

Advance Notice Bylaws

Hill International, Inc. v. Opportunity Partners L.P., 119 A.3d 30 (Del. 2015).

In *Hill International, Inc. v. Opportunity Partners L.P.*, 119 A.3d 30 (Del. 2015), the Delaware Supreme Court affirmed the Court of Chancery's grant of mandatory injunctive relief enjoining Hill International, Inc. ("Hill") from conducting any business at its 2015 annual meeting, other than convening the meeting for the sole purpose of adjourning it for a minimum time period, in order to permit Opportunity Partners ("Opportunity"), the stockholder-plaintiff, to present certain items of business and director nominations at Hill's 2015 annual meeting.

The key issue in the case was whether Opportunity had complied with Hill's advance notice bylaw in submitting its proposed business and nominations. On April 30, 2014, Hill publicly disclosed in its 2014 definitive proxy statement that it anticipated that its 2015 annual meeting would be "on or about June 10, 2015" and that stockholders who wished to submit a proposal for the 2015 annual meeting must submit their proposal no later than April 15, 2015. The following year, on April 13, 2015, Opportunity delivered to Hill a notice of its intent to propose business and nominate two directors at Hill's 2015 annual meeting. On April 30, 2015, Hill filed its definitive proxy statement for its 2015 annual meeting and announced that its 2015 annual meeting would be held on June 9, 2015. Subsequently, on May 5, 2015, Hill asserted that Opportunity's April 13 notice was defective because it failed to include information about the director nominees required by the bylaws. On May 7, Opportunity delivered another notice to Hill of its intent to present at the 2015 annual meeting two different proposals than had been included in its April 13 notice, as well as nominations for election to Hill's board of the same two nominees as had been named in the April 13 letter. On May 11, Hill notified Opportunity that its notice was untimely under Hill's advance notice bylaw and that its proposals and nominations would not be presented at the 2015 annual meeting. Opportunity brought suit in the Court of Chancery claiming its notice was timely under Hill's bylaws.

Unlike many advance notice bylaws where stockholder notice of intent to make nominations or propose business is required to be delivered some number of days prior to the anniversary of the prior year's meeting or the mailing of the prior year's proxy statement, Hill's advance notice bylaw provides:

> To be timely, a stockholders' notice must be delivered to or mailed and received at the principal executive offices of the Corporation not less than sixty (60) nor more than ninety (90) days prior to the meeting; provided, however, that in the event that less than seventy (70) days' notice or prior public disclosure of the date of the annual meeting is given or made to stockholders, notice by a stockholder, to be timely, must be received no later than the close of business on the tenth (10th) day following the day on which such notice of the date of annual meeting was mailed or such public disclosure was made, whichever first occurs.

In support of its contention that Opportunity's notice was untimely, Hill argued that the disclosure in its 2014 definitive proxy statement that the annual meeting would be "on or around June 10, 2015" constituted prior public disclosure of the date of the meeting such that Opportunity was required to notify Hill of its intent to propose business and nominations not less than 60 days prior to the meeting. In response, Opportunity claimed that the first notice of the date of

the meeting—June 9, 2015—was not given until April 30, less than 70 days prior to the date of the annual meeting, such that its May 7 notice was timely.

The Court of Chancery agreed with Opportunity, explaining that, although Hill could have triggered the requirement for at least 60 days' advance notice of proposals and nominations by announcing the specific date of the meeting prior to the filing of its definitive proxy statement, because it did not, Opportunity had 10 days from the date of the filing to submit its notice to Hill. Therefore, because the May 7 notice was timely, the Court of Chancery held that Hill was violating the plain language of its bylaws and that, because Opportunity would suffer irreparable harm absent injunctive relief and the balance of hardships favored Opportunity, Opportunity was entitled to mandatory injunctive relief.

Reviewing the bylaws *de novo,* the Delaware Supreme Court held that Hill's "clear and unambiguous" advance notice bylaw required Hill to provide notice of the specific day—and not a range of possible days —on which the annual meeting was to occur in order to trigger the time periods under the advance notice bylaw. In particular, the Court explained:

> The plain meaning of "the date" means a specific day—not a range of possible days. The 2014 Proxy Statement's reference to "on or about June 10, 2015" does not refer to "the date" of Hill's 2015 Annual Meeting. Rather, "on or about" refers to an approximate, anticipated, or targeted time frame that is intended to encompass more than one "date"—*i.e.,* June 10—apparently in order to give Hill some flexibility in scheduling. Thus, the 2014 Proxy Statement did not provide "prior public disclosure of the date" of Hill's 2015 Annual Meeting.

As such, because Hill did not provide notice of the specific date of its annual meeting until it filed its proxy statement for the 2015 annual meeting on April 30, 2015 announcing the June 9 date, the Court held that Opportunity's May 7 notice was timely.

In affirming the Court of Chancery's grant of mandatory injunctive relief, the Delaware Supreme Court provided additional guidance to practitioners in drafting advance notice bylaws. Notably, the Court suggested that corporations could avoid the situation in which Hill found itself by either pegging the notice period for timely stockholder proposals and director nominees to the anniversary date of the corporation's prior annual meeting or by publicly announcing the specific date of its annual meeting prior to the sending of notice of such annual meeting in the manner required by Section 222 of the Delaware General Corporation Law, which requires, among other things, that such notice be sent not more than 60 days prior to the annual meeting. The Court noted that the Hill board had fixed the June 9, 2015 date of the 2015 meeting on March 12, 2015, but made no announcement when it did so.

Corporations with advance notice bylaws that key the notice period for stockholder proposals and nominations off the current year's meeting date rather than the anniversary of the prior year's annual meeting or the mailing of the prior year's proxy statement should not rely on the statement of anticipated meeting date in the prior year's proxy statement as announcing the meeting date and should make public announcement of the specific meeting date once it has been fixed. Alternatively, to avoid having the window for business proposals and nominations opened after they have filed their proxy materials, corporations may want to consider amending their advance notice bylaws to key the notice period from the anniversary of the prior year's annual meeting or the date of mailing of the prior year's proxy statement.

Fee-Shifting Bylaws

Strougo v. Hollander, 2015 WL 1189610 (Del. Ch. Mar. 16, 2015).

In *Strougo v. Hollander,* 2015 WL 1189610 (Del. Ch. Mar. 16, 2015), the first opinion of the Delaware Court of Chancery to address the validity of a fee-shifting bylaw since the Delaware Supreme Court's opinion in *ATP Tour, Inc. v. Deutscher Tennis Bund,* 91 A.3d 554 (Del. 2014), the Court held that a corporation's fee-shifting bylaw adopted after the consummation of a 10,000-to-1 reverse stock split did not apply to the

stockholders whose entire interest was cashed out in the split. Although noting the "serious policy questions implicated by fee-shifting bylaws in general," the Court based its holding on the timing of the bylaw's adoption. The Court held that the bylaw did not apply to the stockholders whose entire interest had been cashed out in the split, because Section 109 of the DGCL does not authorize a bylaw that "regulates the rights or powers of former stockholders who were no longer stockholders when the bylaw was adopted."

The Court clarified, however, that its conclusion does not mean that a stockholder whose interest in the corporation is eliminated ceases to be subject to the corporation's bylaws. Instead, the Court held that, "[i]n determining the bylaw provisions that should apply to a lawsuit initiated by a former stockholder challenging the terms of a cash-out transaction,…the governing bylaws are those in effect when the former stockholder's interest as a stockholder was eliminated." After that date, a stockholder ceases to be a party to the "corporate contract" and accordingly ceases to be bound by subsequent amendments to that contract.

ATP Tour, Inc. v. Deutscher Tennis Bund, 91 A.3d 554 (Del. 2014).

In *ATP Tour, Inc. v. Deutscher Tennis Bund,* 91 A.3d 554 (Del. 2014), the Delaware Supreme Court, by Justice Berger, in responding to certified questions of law from the United States District Court for the District of Delaware (the "District Court"), held that a provision of a Delaware nonstock corporation's bylaws that shifted litigation expenses to the losing party in intra-corporate litigation was facially valid under Delaware law and may be enforced if the provision was adopted through appropriate corporate procedures and for a proper corporate purpose.

ATP Tour, Inc. ("ATP") is a Delaware nonstock corporation that operates a professional tennis tour. The dispute arose from litigation filed in District Court by the plaintiffs, two members of ATP, against ATP and six of its seven directors challenging ATP's decision to downgrade a tournament owned and operated by the plaintiffs. Following a jury trial, judgment was entered in favor of ATP on all claims. Because the plaintiffs did not prevail on any of their claims, ATP sought to recover its litigation expenses from the plaintiffs pursuant to a provision in ATP's bylaws providing that, in intra-corporate litigation, a plaintiff who "does not obtain a judgment on the merits that substantially achieves, in substance and amount, the full remedy sought" is obligated to reimburse ATP "for all fees, costs and expenses of every kind and description." Because the validity and enforceability of a fee-shifting bylaw presented a novel question of Delaware law, the District Court certified questions to the Delaware Supreme Court.

The Supreme Court began its analysis by noting that, to be facially valid, a bylaw provision must be authorized by the General Corporation Law of the State of Delaware (the "DGCL"), it must be consistent with the corporation's certificate of incorporation, and its enactment must not be otherwise prohibited. Finding that such a bylaw was not prohibited by the DGCL, any other Delaware statute or common law, the Supreme Court held that a fee-shifting bylaw is facially valid under Delaware law. The enforceability of a fee-shifting bylaw, however, turns on the circumstances under which the bylaw is adopted and applied. Because the Court did not have sufficient facts to determine whether ATP's fee-shifting bylaw was properly adopted or applied and because certified questions by their nature only address questions of law, the Supreme Court did not opine on the enforceability of ATP's fee-shifting bylaw. Rather, the Supreme Court held that a fee-shifting bylaw, like the one adopted by ATP, may be enforceable if adopted by appropriate corporate procedures and for a proper corporate purpose. The Court further noted that bylaws that are facially valid will not be enforced if adopted or applied for an inequitable or improper purpose. Because the intent to deter litigation is not invariably an improper purpose, the fact that a board adopted a fee-shifting bylaw for the purpose of deterring litigation would not necessarily render the bylaw unenforceable. Finally, the Court held that, assuming that a fee-shifting bylaw is otherwise valid and enforceable, members who join the corporation prior to its adoption will be bound by the fee-shifting bylaw.

Proposed amendments to the DGCL have been introduced in the Delaware General Assembly to clarify

the application of the *ATP Tour* decision to Delaware stock corporations. If these proposed amendments are approved, they would limit the applicability of the *ATP Tour* decision to nonstock corporations and clarify that, subject to limited statutory exceptions, charter and bylaw provisions may not be used to impose monetary liability on holders of stock in Delaware stock corporations.

For-Cause Removal

In re Vaalco Energy, Inc. Stockholder Litigation, C.A. No. 11775-VCL (Del. Ch. Dec. 21, 2015) (TRANSCRIPT).

In *In re Vaalco Energy, Inc. Stockholder Litigation,* C.A. No. 11775-VCL (Del. Ch. Dec. 21, 2015) (TRANSCRIPT), the Court of Chancery granted the plaintiffs' motion for summary judgment and invalidated certain provisions of Vaalco's certificate of incorporation and bylaws, which provided that members of its board of directors could only be removed for cause. The Court held that the default rule under Section 141(k) of the General Corporation Law of the State of Delaware (the "DGCL") that directors "may be removed, with or without cause" may be limited to removal only for cause solely in corporations that either (i) have a board classified pursuant to Section 141(d) of the DGCL (*i.e.,* a staggered board), or (ii) provide for cumulative voting pursuant to Section 214 of the DGCL.

Before its 2010 annual meeting, Vaalco had a staggered board and provisions in its certificate of incorporation and bylaws mandating that directors could be removed only for cause. In 2010, Vaalco de-staggered its board, but failed to remove the provisions of its certificate and bylaws providing for removal of directors for cause only. After a group of dissident stockholders announced its intention to remove certain members of Vaalco's board in late 2015, Vaalco asserted that these provisions prohibited such action without cause. In response, the group of stockholders brought an action seeking a declaratory judgment that Vaalco's certificate of incorporation and bylaw provisions permitting only for-cause removal of directors were void under Section 141(k).

Section 141(k) provides that "[a]ny director or the entire board of directors may be removed, with or without cause, by the holders of a majority of the shares then entitled to vote at an election of directors" except in the case of a corporation with either (i) a staggered board, or (ii) cumulative voting. The defendants advanced several arguments in favor of the validity of the Vaalco certificate of incorporation and bylaw provisions, including the alleged fact that approximately 175 public Delaware corporations had similar provisions in their governing documents regarding director removal despite lacking a staggered board or cumulative voting. Of these, the Court found most persuasive the defendants' argument that Section 141(d) permits a classified board to "be divided into 1, 2 or 3 classes," and thus allows for a board to be classified into a single class. Accordingly, the defendants argued that a single-class board would be classified for the purposes of Section 141(k), and could properly be subject to removal for cause only.

The Court, however, rejected this argument, which, in its view, would create a "somewhat oxymoronic concept of a single-class classified board." In so holding, the Court relied upon commentary on the 1974 amendments to the DGCL, which explained that the language in Section 141(d) permitting a board to be "divided into 1, 2 or 3 classes" was intended to clarify that the right of any class or series of stock to elect one or more directors would not create an additional class of directors and did not support the notion of a single-class classified board. Additionally, while Vaalco advanced its interpretation of Section 141(d), it never actually established that its board was classified. Thus, the Court alternatively held that, even if Section 141(d) permitted a single-class classified board, Vaalco did not have such a board.

Following the ruling described above, the plaintiffs' bar began sending demand letters to the 175 companies identified by the defendant in Vaalco. Suits have been filed against several of those companies. For companies that have de-staggered their boards within the last several years, it may be worthwhile to determine whether similar issues exist before the plaintiffs' bar initiates contact.

Derivative Actions and Claims

In re El Paso Pipeline Partners, L.P. Deriv. Litig., 2015 WL 7758609 (Del. Ch. Dec. 2, 2015).

In *In re El Paso Pipeline Partners, L.P. Deriv. Litig.,* 2015 WL 7758609 (Del. Ch. Dec. 2, 2015), the Court of Chancery denied a motion to dismiss a suit, in which the Court had already entered a $171 million damages award against the defendants, on the grounds that the plaintiff had lost standing as a result of a post-trial merger. In denying the motion to dismiss, the Court addressed the distinction between direct and derivative claims while offering its view with respect to dual-natured claims.

Through two transactions in 2010, El Paso Corporation ("El Paso Parent"), which owned the sole general partner of El Paso Pipeline Partners, L.P. (the "MLP"), sold two of its subsidiaries to the MLP. The plaintiff filed suit derivatively on behalf of the MLP challenging each of the transactions. After consolidation of the two lawsuits, the Court granted the defendants' motion for summary judgement as to the first transaction. However, trial was held with respect to the second transaction (the "Fall Dropdown"), following which the Court found that the Fall Dropdown did not receive "special approval" (as defined in the MLP's operating agreement) because the members of the MLP's conflicts committee had failed to form a subjective belief that the transaction was in the best interests of the MLP. Accordingly, the Court found that approval of the Fall Dropdown had breached the partnership agreement and awarded $171 million in damages, the amount of overpayment caused by the breach.

During the pendency of the litigation, Kinder Morgan Inc. acquired El Paso Parent. Shortly after trial Kinder Morgan, El Paso Parent, the MLP, and El Paso Pipeline GP Company, L.L.C. ("El Paso General Partner") consummated a related-party merger, which brought an end of the separate legal existence of the MLP. El Paso General Partner then moved to dismiss the lawsuit on the basis that the plaintiff's claims were exclusively derivative and the plaintiff lacked standing to pursue his claims due to the merger.

The Court rejected the motion to dismiss and found that to the extent Delaware law required it to make a choice between construing the plaintiff's claim as either exclusively derivative or exclusively direct, the claim was direct in nature. The Court reasoned that the plaintiff had proved that El Paso General Partner violated certain provisions of the MLP's partnership agreement, a contract to which the plaintiff and the other limited partners of the MLP were parties. The Court stated that "[g]ranting the motion to dismiss would generate a windfall for the general partner at the expense of the unaffiliated limited partners for whose indirect benefit this suit originally was brought." The Court relied on the public policy underlying the limited partnership statute to give maximum effect to the principle of freedom of contract and enforceability of partnership agreements in finding that limited partners can sue directly to enforce contractual constraints in a limited partnership agreement.

However, the Court declined to accept the defendants' "bipolar" view of classification of the plaintiff's claim as either exclusively direct or exclusively derivative. Instead the Court suggested that the "more appropriate way" to view the claim is as dual-natured, with aspects that are both direct and derivative. In reaching this conclusion, the Court analyzed the claim under the two-part *Tooley* test. The Court found the analysis under *Tooley* straightforward if the claim were considered one for breach of contract: the limited partners suffered a breach of their contract rights and that breach could be remedied appropriately at the limited partner level. The Court also held that, even setting aside the contractual nature of the claim, the claim was both direct and derivative under *Tooley*. Specifically, the first prong of the *Tooley* test, adapted for a limited partnership, asks who suffered the alleged injury, the partnership or the limited partners individually. The Court held, in the context of the plaintiff's claim, the answer was both, because the MLP and its limited partners suffered injuries resulting from El Paso General Partner's breach of the MLP's partnership agreement. The MLP suffered by overpaying in the Fall Dropdown, and the

limited partners suffered because the transaction effectively reallocated value from them to El Paso General Partner. The second prong of the *Tooley* test asks who would receive the benefit of any remedy, the partnership or the limited partners individually. The Court determined the answer to this second question was either, because Delaware law supported both an entity-level remedy and a limited partner-level remedy with respect to overpayment claims. Therefore, the Court concluded that the plaintiff's claim was dual-natured and could be pursued directly or derivatively.

In dicta, the Court also expressed its view that the treatment of dual-natured claims is an area of Delaware law that warrants further development. Specifically, the Court suggested that when considering how a dual-natured claim should be treated for purposes of whether it can be maintained after a merger, Delaware law should prioritize the individual aspects of the claim such that it survives. However, when considering how a dual-natured claim should be treated for purposes of determining demand futility, Delaware law should prioritize the derivative aspects of the claim. This would preserve the policy goals of screening out meritless claims and protecting the primacy of the board's (or other manager's) management of the entity.

Finally, the Court rejected El Paso General Partner's estoppel argument, finding Delaware law is clear that a plaintiff's characterization of its claims as either direct or derivative is not binding on the Court. The Court ruled that the plaintiff can continue to pursue the claim after the merger and can enforce the $171 million judgment. The Court ordered the current general partner to pay the MLP's unaffiliated limited partners as of the time of the merger their pro rata share of the $171 million award, plus pre- and post-judgment interest through the date of payment, less an amount for a reasonable award of attorneys' fees and expenses.

In re Molycorp, Inc. Shareholder Derivative Litigation, 2015 WL 3454925 (Del. Ch. May 27, 2015).

In *In re Molycorp, Inc. Shareholder Derivative Litigation,* 2015 WL 3454925 (Del. Ch. May 27, 2015), the Court of Chancery granted under Rule 12(b)(6) the defendants' motions to dismiss a derivative complaint that alleged breaches of fiduciary duties, among other claims, in connection with a secondary stock offering that was initiated at the request of Molycorp, Inc.'s private equity investors pursuant to the terms of a Registration Rights Agreement.

In 2010, before Molycorp's initial public offering, certain private equity investors executed a Stockholders Agreement and a Registration Rights Agreement with the company. The Stockholders Agreement granted the investors the right, among others, to nominate directors to Molycorp's board. The Registration Rights Agreement granted the investors a contractual right to have Molycorp register their shares for a secondary offering upon demand by the private equity investors. Under the Registration Rights Agreement, the private equity investors were also granted the right to have their shares given priority over any shares offered by the company in a secondary offering.

In 2011, the private equity investors invoked their rights under the Registration Rights Agreement to cause Molycorp to offer their shares in a secondary offering. In the offering, the private equity investors and certain directors of Molycorp sold shares of Molycorp stock at $51 per share, generating approximately $575 million. Molycorp, on the other hand, conducted a private offering of convertible notes, which raised only $223 million. During this period, as the plaintiffs alleged in the complaint, Molycorp was in financial distress and in need of capital. At the time of the challenged secondary offering, the private equity investors owned approximately 44% of the company's outstanding stock and had nominated four directors. As result, the plaintiffs asserted that the private equity investors and the company's directors breached their fiduciary duties by favoring the interests of certain private equity stockholders over the interests of the company. Among other arguments, the plaintiffs asserted that the board should have delayed the secondary offering and allowed Molycorp to make its own offering in order to raise capital.

The defendants moved to dismiss the plaintiffs' complaint pursuant to Court of Chancery Rule 23.1 for failure to make a demand on the board of directors and pursuant to Court of Chancery Rule 12(b)(6) for failure

to state a claim. Because the Court dismissed the complaint for failure to state a claim, it did not address the defendants' Rule 23.1 arguments, nor did it decide which standard of review applied to the breach of fiduciary duty claims. The Court, however, assumed without deciding that a majority of the directors had disqualifying interests by reason of personal gains or fiduciary relationships with the private equity investors and that demand would be excused.

In opposition to the motions to dismiss, the plaintiffs asserted that the defendants sold their stock and prevented the company from participating in the secondary offering at a time when Molycorp needed funding. The Court rejected the plaintiffs' argument and observed that "[a]ppointment by a powerful shareholder does not automatically render a director's decision suspect" and that it is not wrong, without more, for a director to buy or sell company shares. Indeed, the Court noted, "[i]f such conduct were actionable, 'directors of every Delaware corporation would be faced with the ever-present specter of suit for breach of their duty of loyalty if they sold stock in the company on whose Board they sit.'"

In granting the defendants' motions to dismiss, the Court observed that the Registration Rights Agreement informed the context in which the defendants were acting and could not be ignored. Importantly, the plaintiffs did not contend that the Registration Rights Agreement was invalid or unenforceable. Instead, the plaintiffs essentially argued that Molycorp's board of directors should have interfered with the private equity investors' contractual rights. The Court declined to accept the plaintiffs' argument. Indeed, the Court noted that "[a] finding otherwise could discourage would-be investors from funding start-ups for fear that their investment value will not be preserved despite disclosed, carefully negotiated agreements." Accordingly, the Court granted the defendants' motions to dismiss.

Quadrant Structured Products Company, Ltd. v. Vertin, 115 A.3d 535 (Del. Ch. May 4, 2015).

In *Quadrant Structured Products Company, Ltd. v. Vertin,* 115 A.3d 535 (Del. Ch. May 4, 2015), the Delaware Court of Chancery denied the defendants' motion for summary judgment, held that Delaware law imposes neither a continuous insolvency nor an irretrievable insolvency requirement, and found sufficient evidence in the record to support a reasonable inference that the debtor corporation was insolvent on the date the complaint was filed. In so holding, the Court provided an in-depth analysis of creditor derivative standing following the Delaware Supreme Court's decision in *N. Am. Catholic Educ. Programming Found., Inc. v. Gheewalla,* 930 A.2d 92 (Del. 2007).

The individual defendants are members of the board of directors of the corporate debtor, Athilon Capital Corp. Athilon's equity is wholly owned by defendant Merced Capital LP. Plaintiff Quadrant Structured Products Company, Ltd. is an owner of debt securities issued by Athilon. In this action, Quadrant alleged that following Merced's acquisition of Athilon, the board took numerous actions to benefit Merced at the expense of Athilon's other stakeholders. In February 2015, the defendants moved for summary judgment on the theory that Athilon had returned to solvency and Quadrant therefore had lost standing to pursue any derivative claims.

The Court first analyzed in depth Delaware law on creditor breach of fiduciary duty claims, both before and after *Gheewalla*. The Court concluded that *Gheewall*a and the cases following it implemented a new regime in evaluating such claims. The current regime holds that there is no longer any zone of insolvency, no cause of action for deepening insolvency, and no fiduciary duties owed directly to creditors. Therefore, after *Gheewalla,* there is no need under Delaware law for derivative standing hurdles that may be "unnecessary and counterproductive impediments to the effective use of the derivative action as a meaningful tool for oversight." Directors of Delaware corporations are already sufficiently protected by other aspects of Delaware law.

In addressing the defendants' argument that Delaware law should recognize a continuous insolvency requirement, the Court also looked to the purposes of a derivative action. Derivative suits are intended to remedy wrongdoing by directors and allow equitable owners to increase the company's value. Creditors share each of those incentives when a company is insolvent, and continue to have such incentives as long

as they remain a creditor of the company. Thus, the Court concluded that the proper analogy in the creditor derivative context is a continuous creditor requirement, not a continuous insolvency requirement. In addition, the Court found that depriving creditors of standing to pursue derivative claims on behalf of a company that goes back and forth over the insolvency line while the equity is owned entirely by one stockholder would lead to a "failure of justice" because conflicted fiduciaries could prevent the corporation or its stockholders from pursuing valid claims.

For these reasons, among others, the Court held that "to maintain a derivative claim, the creditor-plaintiff must plead and later prove that the corporation was insolvent at the time suit was filed. The creditor-plaintiff need not, however, plead and prove that the corporation was insolvent continuously from the time of suit through the date of judgment." Finally, the Court also held that the proper test to assess creditor derivative standing at the time the litigation is filed is to determine whether the company "has liabilities in excess of a reasonable market value of its assets." While this test potentially conflicts with certain passages quoted in *Gheewalla,* which were originally written in the receivership context, the Court drew a distinction between claims in the receivership setting and fiduciary duty claims of creditors. Using this test, Quadrant's showing that Athilon's GAAP balance sheet showed a $300 million negative equity value was sufficient to create an issue of material fact as to Athilon's solvency at the time suit was filed.

Quadrant Structured Products Company, Ltd. v. Vertin, 102 A.3d 155 (Del. Ch. Oct. 1, 2014); ***Quadrant Structured Products Company, Ltd. v. Vertin,*** 2014 WL 5465535 (Del. Ch. Oct. 28, 2014).

In *Quadrant Structured Products Company, Ltd. v. Vertin,* 102 A.3d 155 (Del. Ch. Oct. 1, 2014), the Delaware Court of Chancery held that the contemporaneous ownership requirement of Section 327 of the General Corporation Law of the State of Delaware (the "DGCL") does not apply to corporate creditors for purposes of determining whether a creditor has standing to bring derivative claims against the board of directors of an insolvent corporation. The Court also declined to dismiss the creditor's fiduciary duty and fraudulent transfer claims related to certain transactions between the corporation and its controlling stockholder, but granted the motion to dismiss with respect to fiduciary duty claims related to the decision of the board of directors to pursue a "risk-on" business strategy that allegedly favored junior creditors over more senior creditors.

The individual defendants were members of the board of directors of Athilon Capital Corp. ("Athilon") that were allegedly controlled by EBF & Associates ("EBF"), Athilon's sole stockholder and the holder of junior notes issued by Athilon (the "Junior Notes"). The plaintiff, Quadrant Structured Products Company, Ltd. ("Quadrant"), owned debt securities issued by Athilon that were senior to the Junior Notes held by EBF. Quadrant alleged that the EBF-controlled board took a number of actions while Athilon was insolvent to benefit EBF at the expense of its other stakeholders, including (i) paying interest on the Junior Notes instead of deferring the payments to future periods as permitted by the terms of the Junior Notes, (ii) entering into certain agreements with EBF's affiliates at above-market rates, and (iii) amending the limited purpose provisions in Athilon's certificate of incorporation to allow Athilon to pursue a riskier business model that allegedly preferred the interests of EBF over more senior creditors.

As a preliminary matter, the Court held that Quadrant, as a creditor of Athilon, had standing to pursue its claims derivatively. The Court clarified that the fact of insolvency does not give rise to any special duty that is owed by a board of *directors directly to the corporation's creditors,* but rather gives the corporation's creditors derivative standing to enforce the general fiduciary duty that the board of directors owes *to the corporation* to maximize the firm's value for all residual claimants. In addition, the Court declined to extend the contemporaneous ownership requirement of Section 327 of the DGCL to creditors, thereby holding that creditors are not prevented from bringing derivative claims in respect of transactions that pre-date the corporation's insolvency or their acquisition of an insolvent corporation's debt. Although the argument

was not raised by the defendants, the Court noted that it is possible that creditors could be required to comply with other substantive principles of derivative actions, such as demand excusal and demand refusal, in order to pursue derivative claims.

With respect to Quadrant's substantive claims, the Court found that Quadrant's allegations adequately stated a claim for breach of fiduciary duty and fraudulent transfer with respect to the payment of interest on the Junior Notes and the agreements with EBF's affiliates. Furthermore, because EBF was a controlling stockholder that allegedly stood on both sides of the transactions, the Court held that the transactions would be subject to scrutiny under the entire fairness standard of review. The Court dismissed Quadrant's claims with respect to the board's decision to pursue a riskier business strategy, finding that the directors had made decisions that appeared rationally designed to increase the value of the firm as a whole rather than impermissibly preferring the interests of EBF, as a junior creditor and stockholder, to the interests of other residual claimants. Finally, the Court concluded that none of the directors could invoke the protections of the exculpatory provision in Athilon's certificate of incorporation because three of the directors were officers of either Athilon or EBF and it was not possible at the motion to dismiss stage of the proceeding to determine whether any breach of fiduciary duty on the part of the other two directors resulted solely from a breach of the duty of care.

In a decision issued less than one month later, the Court of Chancery, in *Quadrant Structured Products Company, Ltd. v. Vertin,* 2014 WL 5465535 (Del. Ch. Oct. 28, 2014), denied Quadrant's motion for reconsideration of the dismissal of claims related to the board's risk-on strategy. Quadrant contended that the Court had overlooked the importance of the fact that Athilon was a limited purpose corporation and that pursuing the riskier business strategy was outside the scope of its original purpose, as set forth in its certificate of incorporation. Quadrant also argued that the Court had failed to consider whether its allegations were sufficient to support an inference of bad faith and rebut the business judgment rule with regard to the board's decision to amend the corporation's certificate of incorporation in order to pursue the riskier strategy. The Court noted that Quadrant's first argument did not present grounds for reconsideration because Quadrant's own complaint established that Athilon's governing documents authorized the board's risk-on strategy. Specifically, the complaint recognized that the board had the authority to amend Athilon's certificate of incorporation and thus could expand Athilon's limited purpose to make investments involving greater risk. With respect to Quadrant's second argument, the Court noted that the motion to dismiss opinion considered and rejected Quadrant's bad faith claims when it held that the board had made a rational business decision to pursue a riskier investment strategy.

Section 205 Actions

In re Genelux Corporation, 126 A.3d 644 (Del. Ch. 2015); ***In re Baxter International Inc.,*** C.A. No. 11609-CB (Del. Ch. Jan. 15, 2016) (TRANSCRIPT).

Two recent decisions by the Delaware Court of Chancery have helped to define the contours of the Court's authority in proceedings under Section 205 of the General Corporation Law of the State of Delaware (the "DGCL"). In *In re Genelux Corporation,* 126 A.3d 644 (Del. Ch. 2015), the Court of Chancery held that a corporation cannot use Section 205 to invalidate prior corporate acts, and in *In re Baxter International Inc.,* C.A. No. 11609-CB (Del. Ch. Jan. 15, 2016) (TRANSCRIPT), the Court of Chancery held that a corporation cannot use Section 205 as a means to ensure the validity of future corporate acts.

Section 205, which became effective April 1, 2014, and was amended effective August 1, 2015, confers jurisdiction on the Court of Chancery to determine the validity of defective corporate acts and stock issuances. Since Section 205 was enacted in 2014, the Court of Chancery has used its powers under Section 205 to resolve issues relating to a corporation's valid existence, including confirming the identity of the members of the corporation's board of directors (*see In re Trupanion,* C.A. No. 9496-VCP (Del. Ch. Apr. 28, 2014) (ORDER)), and to validate defective stock issuances (*see In re Numoda*

Corporation Shareholders Litigation, C.A. No. 9163-VCN (Del. Ch. Jan. 30, 2015), and *In re CertiSign Holding, Inc.,* C.A. No. 9989-VCN (Del. Ch. Aug. 31, 2015)). However, both *Genelux* and *Baxter* involved unique petitions that had the potential to expand the scope of the Court of Chancery's authority under Section 205 beyond the validation of past defective corporate acts.

In *Genelux,* Genelux Corporation ("Genelux") petitioned the Court of Chancery to invalidate 1.5 million shares of Genelux's Series A Preferred shares (the "Disputed Shares") that Genelux purportedly issued to Aladar Szalay, one of Genelux's founders ("Szalay"), under Section 205 and to declare the elections of two directors invalid under Section 225 of the DGCL as a result of the invalid issuance of the Disputed Shares. Genelux claimed that the Disputed Shares were invalid because, among other things, (i) the Disputed Shares were allegedly issued in exchange for shares of Genelux common stock that were invalid; (ii) Szalay released his claim to the Disputed Shares in a settlement of litigation with a third party; (iii) the issuance of the Disputed Shares was not supported by valid consideration; and (iv) Genelux was fraudulently induced by Szalay to issue the Disputed Shares.

Before reaching the merits of Genelux's claims with respect to the validity of the Disputed Shares, the Court of Chancery addressed the threshold issue of whether Section 205 can be used to invalidate purportedly defective corporate acts. Genelux argued that because Section 205(a)(4) authorizes the Court of Chancery to determine the validity of any stock (and not just putative or defective stock), the Court of Chancery should have the ability to determine that the stock subject to the petition is invalid. Szalay argued that Section 205, when read as a whole, only granted the Court of Chancery the power to validate defective stock issuances, not stock issuances that have been treated by the corporation as valid as evidenced by, in this case, the issuance of stock certificates, entries in the corporate stock ledger and board resolutions. The Court of Chancery found that the plain language of Section 205 was ambiguous as to whether the Court of Chancery is permitted to invalidate corporate acts. Accordingly, the Court looked to extrinsic evidence—including the legislative synopsis of House Bill 127 (which became Section 205 and Section 204 of the DGCL), the other provisions of Section 204 and Section 205, and commentary in Delaware law treatises concerning Section 205—to resolve the ambiguity.

After reviewing these materials, the Court of Chancery concluded that Section 205 is a "remedial statute" that was only designed to "cure otherwise incurable defective corporate acts, not a statute to be used to launch a challenge to stock issuances on grounds already available through the assertion of plenary-type claims based on alleged fiduciary duty or common law fraud or a Section 225 action, if the stock had been voted." Thus, the Court of Chancery dismissed for failure to state a claim Genelux's petition under Section 205 seeking a declaration that the Disputed Shares were invalid. The Court of Chancery also dismissed Genelux's Section 225 claims, concluding that (i) Genelux had failed to prove by a preponderance of the evidence that it did not approve the issuance of the shares of common stock for which the Disputed Shares were exchanged; (ii) the settlement did not include a general release of claims that Szalay may have against Genelux; (iii) the exchange of the shares of common stock and Szalay's release of his claims to additional shares of Genelux constituted valid consideration for the issuance of the Disputed Shares; and (iv) Szalay's conduct in pressing Genelux to issue the Disputed Shares in connection with an unrelated third-party financing did not rise to the level of fraud.

In *Baxter,* the certificate of incorporation of Baxter International Inc. ("Baxter") contained a provision that stated that Article SIXTH of the certificate of incorporation could not be amended without the vote of at least "two-thirds of the holders of all the securities of [Baxter] then entitled to vote on such change" (the "voting provision"). Baxter planned to seek an amendment of Article SIXTH at its upcoming annual meeting, and its board of directors adopted a resolution (the "voting resolution") stating that the board had determined to count votes on the amendment on a "per share basis, rather than on a per capita basis," even though the voting provision, on its face, seemed to call for a per capita vote and previous public disclosures indicated that Baxter had counted votes subject to the provision on a per capita basis in the past. Baxter filed a petition with

the Court of Chancery under Section 205 requesting that the Court validate the voting resolution as well as the voting standard set forth in the voting resolution. In effect, Baxter requested the Court to declare that the voting resolution properly provided that the upcoming vote on the amendment to the certificate should be determined on a per share basis, rather than a per capita basis. Although Baxter's Section 205 petition was initially unopposed, the Court of Chancery appointed Richards, Layton & Finger as special counsel to file an opposition brief if no stockholder came forward to oppose the petition after notice was given.

The Court of Chancery, issuing its ruling from the bench after oral argument, distinguished between determining the validity of the voting resolution itself and determining the proper voting standard for the proposed certificate amendment. The Court of Chancery indicated that it could address under Section 205 the validity of the voting resolution if there had been some defect in its adoption (for example, if it was not adopted by a sufficient number of directors), but that Section 205 did not permit the Court to provide an opinion on the underlying contents of the voting resolution.

Moreover, the Court of Chancery determined that Section 205 did not empower the Court to validate future corporate acts. While Baxter argued that a corporate act had already occurred because the board had adopted the voting resolution, the Court of Chancery pointed out that the annual meeting where the vote on the amendment was to occur had not been held and might never occur. The Court of Chancery likened Baxter's Section 205 petition to a request for an advisory opinion on an unripe issue and dismissed the case. However, the Court of Chancery acknowledged that Section 205 is a flexible statute "intended to promote equitable outcomes and to provide certainty to stockholders," and that relief under Section 205 may be possible under appropriate circumstances. The Court of Chancery noted that if Baxter held its annual meeting, received sufficient votes counted on a per-share basis to amend, and actually amended its certificate of incorporation on that basis, Baxter would have a stronger argument that the Court should validate the amendment under Section 205 because a corporate act actually would have occurred. ■

Removal of Officers

Gorman v. Salamone, 2015 WL 4719681 (Del. Ch. July 31, 2015).

In *Gorman v. Salamone,* 2015 WL 4719681 (Del. Ch. July 31, 2015), the Delaware Court of Chancery held that a stockholder-adopted bylaw amendment that purported to grant stockholders the authority to remove corporate officers over the objection of the corporation's board of directors was invalid under Delaware law. In so holding, the Court found that the amended bylaw, which permitted stockholders to remove and replace officers without cause, would allow stockholders to "make substantive business decisions" for the corporation and thereby "unduly interfere with directors' management prerogatives" under Section 141(a) of the General Corporation Law of the State of Delaware (the "DGCL").

The Court of Chancery's opinion in *Gorman* is the most recent installment in an ongoing dispute over the composition of the board of directors of Westech Capital Corp. (the "Company" or "Westech"). *See In re Westech Capital Corp.,* 2014 WL 2211612 (Del. Ch. May 29, 2014) (designating a four-member board and determining the composition thereof), *aff'd in part, rev'd in part sub. nom. Salamone v. Gorman,* 106 A.3d 354 (Del. 2014) (designating a five-member board and determining the composition thereof). Critical to both the Court of Chancery's earlier post-trial opinion and the Delaware Supreme Court's opinion on appeal was the operation of a voting agreement that required the stockholders party thereto to vote, or cause to be voted, their shares of stock to elect as directors the individuals designated in the manner provided in the agreement. In this respect, the voting agreement provided, among other things, for the election of the Company's chief executive officer as a director, provided that if for any reason the chief executive officer were to cease to serve as the chief executive officer, the stockholders party to the agreement were required to vote their shares to remove the chief executive officer from the board and to elect the new chief executive officer to the board.

Following the Court of Chancery's earlier post-trial opinion, John Gorman, as the Company's majority stockholder, acted by written consent to amend the bylaws of the Company to provide, among other things, that "[a]ny officer may be removed, with or without cause, at any time by the board or by the stockholders acting at an annual or special meeting or acting by written consent pursuant to Section 2.8 of these Bylaws. The Board shall, if necessary, immediately implement any such removal of an officer by the stockholders." In reliance on the amended bylaw, Gorman then removed Gary Salamone as the Company's chief executive officer and elected himself to fill the resulting vacancy. Following his appointment as chief executive officer, Gorman sought to appoint a new director to serve in his newly vacant director seat. Thereafter, Gorman filed suit in the Court of Chancery seeking confirmation that, among other things, Salamone was no longer the chief executive officer or a director of the Company.

The Court of Chancery held that the amended bylaw was invalid, stating that "Delaware law does not allow stockholders to remove directly corporate officers through authority purportedly conferred by a bylaw." The Court of Chancery rejected Gorman's argument that Section 142(b) of the DGCL (providing that "[o]fficers shall be chosen in such manner…as [is] prescribed by the bylaws or determined by the board of directors") and Section 142(e) of the DGCL (providing that "[a]ny vacancy occurring in any office…shall be filled as the bylaws provide") permitted the adoption of a bylaw that would allow stockholders to remove and replace officers. In this regard, the Court explained that neither Section 142(b) nor Section 142(e) expressly provided guidance on how officers may be removed, but only on the *manner* in which officers could be selected and the *manner* in which any vacancy in an office could be filled. Thus, the Court found that the amended bylaw was not authorized by Section 142 of the DGCL. In reaching this conclusion, the Court noted that, prior to its 1967 revision, the DGCL explicitly authorized directors or stockholders to elect corporate officers, and notes that Professor Earnest

Folk, in the first edition of his treatise on the DGCL, commented that the 1967 revision intended no substantive change. That commentary stated that, while the phrase "by directors or officers" was deleted and the phrase "in the manner provided by the bylaws" was added, the changes were not intended to effect any substantive change as to who may choose the officers.

Turning to the argument that stockholders generally have the power under Section 109 of the DGCL to adopt and amend bylaws "relating to the business of the corporation, the conduct of its affairs, and its rights or powers or the rights or powers of its stockholders, directors, officers or employees," the Court nonetheless held that the amended bylaw was outside the scope of bylaws permitted by Section 109. In particular, the Court noted that the amended bylaw required the board to "immediately implement any such removal of an officer by the stockholders," thereby allowing the stockholders to remove an officer over the objection of the board. Explaining that such a directive, if enforceable, "could compel board action, potentially in conflict with its members' fiduciary duties," the Court held that the "stockholders' right to remove officers for any (or no) reason would unduly constrain the board's ability to manage the Company." As a result of such undue constraint, the Court held that the amended bylaw was invalid and that any actions taken in reliance thereon, including the removal of Salamone as chief executive officer, were of no effect.

Notably, the amended bylaw also provided that "[a]ny vacancy occurring in any elected office of the Corporation may be filled by the board except that any such vacancy occurring as a result of the removal of an officer by the stockholders shall be filled by the stockholders." The Court of Chancery expressly declined to address the validity of this provision, stating that "[t]he Court need not (and does not) analyze [the vacancy-filling] aspect of the Amended Bylaw because its validity is irrelevant to the matter at hand." The Court noted, however, that "[p]ermitting stockholders to set the mode for officer replacement would allow them to dictate a procedure, and would not necessarily step unduly on management's toes."

Section 220 Actions

Amalgamated Bank v. Yahoo! Inc., 2016 WL 402540 (Del. Ch. Feb. 2, 2016).

In a post-trial decision, the Court of Chancery ordered respondent Yahoo! Inc. to produce additional documents in response to plaintiff Amalgamated Bank's demand to inspect Yahoo's books and records pursuant to 8 *Del. C.* § 220. *Amalgamated Bank v. Yahoo! Inc.*, 2016 WL 402540 (Del. Ch. Feb. 2, 2016). In doing so, the Court interpreted Section 220 to provide for the production of electronically stored information in addition to physical documents.

The facts centered on Yahoo's hiring of Henrique de Castro as its chief operating officer in October 2012 and de Castro's subsequent termination just 14 months later. The Court of Chancery examined the details surrounding: (i) the involvement of Yahoo's board of directors and compensation committee in the hiring process, (ii) the value of de Castro's compensation package, (iii) the termination of de Castro, (iv) the payout de Castro received upon termination, and (v) the alleged unilateral involvement of Yahoo's CEO, Marissa Mayer, in the hiring and firing of de Castro and the construction of his compensation package.

Amalgamated filed its first demand for inspection of Yahoo's books and records on February 24, 2014, for the purpose of investigating "potential mismanagement, including mismanagement in connection with the payment of compensation to a corporation's officers and directors." Throughout 2014, Amalgamated and Yahoo engaged in negotiations surrounding the demand, and Yahoo eventually produced 677 pages of documents. When Yahoo denied Amalgamated's demand for additional categories of documents, Amalgamated filed suit on March 10, 2015.

The Vice Chancellor's opinion offers clarification on what is sufficient to meet the statutory "form and manner" requirements necessary for bringing a books and records demand under 8 *Del. C.* § 220. Yahoo argued that Amalgamated failed to prove that it owned

Yahoo stock at the time the demand was filed because the proof submitted by Amalgamated was dated three days before the date demand was made—as opposed to being dated the same day as the demand—but the Court rejected that argument. The Vice Chancellor ruled that Section 220 only requires "documentation sufficient in time to the date of demand as to be consistent with and corroborate the averment of stock ownership made in the demand itself." Additionally, the Court found that Amalgamated was not required to provide Yahoo with an ongoing stream of ownership records to confirm continuous ownership of stock.

The Court also analyzed the sufficiency of Amalgamated's stated purpose of demanding inspection of Yahoo's books and records to investigate potential corporate wrongdoing in connection with de Castro's hiring and firing. Distinguishing *Se. Pa. Transp. Auth. v. Abbvie, Inc.,* 2015 WL 1753033 (Del. Ch. Apr. 15, 2015), *aff'd,* 2016 WL 235217 (Del. Jan. 20, 2016), the Court held that Amalgamated had not limited its stated purposes to investigating potential causes of action that would be subject to exculpation, but rather had met the "credible basis" standard with respect to its potential claims for breach of the duty of good faith and waste.

The Court then turned to the scope of inspection. Amalgamated sought production of emails and other files of Yahoo's CEO, Marissa Mayer. The Court found that "[t]he evidence establishes that the Mayer Documents are necessary for a meaningful investigation of de Castro's hiring," due to the direct and personal involvement Mayer had with the negotiations and hiring of de Castro. The Court reached a similar conclusion with regard to Mayer's documents relating to de Castro's termination. The Court ruled that the "scope of the production of the Mayer Documents will include email and other electronic documents, which count as corporate books and records." The Vice Chancellor rejected Yahoo's argument that such documents are not subject to 8 *Del. C.* § 220 because the language of the statute does not explicitly mention electronic information. The Court reasoned that "[a]s with other categories of documents subject to production under Section 220, what matters is whether the record is essential and sufficient to satisfy the stockholder's proper purpose, not its source." The Court further clarified that the production of Mayer's emails should include emails from any personal account she may have used to conduct Yahoo business.

The Vice Chancellor also ordered Yahoo to produce emails and other electronically stored documents in the possession of the members of Yahoo's compensation and leadership development committee, to the extent those documents related to de Castro's hiring or termination. The Court also ordered additional production of documents relating to Yahoo's director recruitment process.

The Court rejected Amalgamated's request for production of documents reflecting consultations with counsel. Recognizing that those documents could be subject to production, notwithstanding the attorney-client privilege and work-product doctrine, under *Garner v. Wolfinbarger,* 430 F.2d 1093 (5th Cir. 1970), the Court determined that it would require Yahoo to log communications with counsel relating to the subjects of the inspection, to the extent those communications were identified in searching for documents produced pre-litigation or in response to the Court's order. The Court left open the possibility that Amalgamated might later show that these privileged documents might be essential to the proper purpose of inspection.

Finally, on an issue of first impression, the Vice Chancellor found that any further document production by Yahoo "is conditioned on Amalgamated agreeing that the entirety of Yahoo's production in response to the Demand is incorporated by reference in any derivative action complaint it files relating to the subject matter of the demand." The Court explained the basis for this condition as a means to protect Yahoo and the Court from the filing of a complaint based on "cherry-picked documents," and to prevent Amalgamated from forging a complaint based on a few documents taken out of context. ■

In re Cornerstone Therapeutics Inc. Stockholder Litigation, 115 A.3d 1173 (Del. 2015).

In *In re Cornerstone Therapeutics Inc. Stockholder Litigation,* 115 A.3d 1173 (Del. 2015), the Delaware Supreme Court resolved two consolidated interlocutory appeals. In the underlying cases (*In re Zhongpin Inc. Stockholders Litigation,* 2014 WL 6735457 (Del. Ch. Nov. 26, 2014), and *In re Cornerstone Therapeutics Inc. Stockholder Litigation,* 2014 WL 4418169 (Del. Ch. Sept. 10, 2014)), the Court of Chancery refused to dismiss independent directors because the governing standard of review was held to be entire fairness.

The Supreme Court reversed and remanded, holding that a "plaintiff seeking only monetary damages must plead non-exculpated claims against a director who is protected by an exculpatory charter provision to survive a motion to dismiss, regardless of the underlying standard of review for the board's conduct—be it *Revlon, Unocal,* the entire fairness standard, or the business judgment rule." Therefore, even in a situation where entire fairness applies *ab initio,* independent directors may seek dismissal under a charter provision authorized by 8 *Del. C.* § 102(b)(7) where the plaintiffs are solely seeking monetary relief.

In re KKR Financial Holdings LLC Shareholder Litigation, 101 A.3d 980 (Del. Ch. 2014); ***In re Crimson Exploration Inc. Stockholder Litigation,*** 2014 WL 5449419 (Del. Ch. Oct. 24, 2014); ***In re Sanchez Energy Derivative Litigation,*** 2014 WL 6673895 (Del. Ch. Nov. 25, 2014); ***In re Zhongpin Inc. Stockholders Litigation,*** 2014 WL 6735457 (Del. Ch. Nov. 26, 2014); ***In re Cornerstone Therapeutics Inc. Stockholder Litigation,*** 2014 WL 4418169 (Del. Ch. Sept. 10, 2014).

In four opinions issued within three months of one another, four different members of the Delaware Court of Chancery have considered, at the motion to dismiss procedural stage, whether allegations in a

complaint were sufficient to establish that a minority stockholder constituted a controlling stockholder under Delaware law. In *In re KKR Financial Holdings LLC Shareholder Litigation,* 101 A.3d 980 (Del. Ch. 2014), *In re Crimson Exploration Inc. Stockholder Litigation,* 2014 WL 5449419 (Del. Ch. Oct. 24, 2014), and *In re Sanchez Energy Derivative Litigation,* 2014 WL 6673895 (Del. Ch. Nov. 25, 2014), the Court concluded that the minority stockholder at issue did not constitute a controlling stockholder, while in *In re Zhongpin Inc. Stockholders Litigation,* 2014 WL 6735457 (Del. Ch. Nov. 26, 2014), the Court found that allegations that a minority stockholder controlled a company and its board of directors were sufficient to withstand a motion to dismiss.

KKR Financial involved a suit challenging the acquisition of KKR Financial Holdings LLC ("KFN") by KKR & Co. L.P. ("KKR"). The Court held that KKR, which owned less than 1% of KFN's stock, was not a controlling stockholder despite allegations that a KKR affiliate managed the day-to-day business of KFN and that KFN was used primarily as a public vehicle for financing KKR-sponsored transactions. In dismissing the complaint, the Court focused on whether KKR had the ability to control the board of directors of KFN and found that the complaint lacked any allegation that KKR had a contractual right to appoint members of the board of directors, that KKR dictated any specific course of action to the board of directors, or that KKR prevented the members of the board of directors from exercising their judgment in determining whether or not to approve the merger with KKR. Accordingly, the Court held that the plaintiffs had failed to demonstrate that it was reasonably conceivable that KKR was a controlling stockholder under Delaware law and dismissed the complaint.

In *Crimson Exploration,* the plaintiffs alleged that Oaktree Capital Management and its affiliates ("Oaktree") collectively controlled Crimson Exploration Inc. ("Crimson") based on Oaktree's ownership of 33.7% of Crimson's voting stock, its status as a large creditor of Crimson, and its designation of a majority of Crimson's directors and senior management (including three directors employed by Oaktree). After reviewing relevant Delaware precedent, the Court explained that a minority stockholder will not be considered a controlling stockholder unless the minority stockholder actually controls the board's decisions about the challenged transaction. The Court then found that the complaint had failed to plead specific allegations that Oaktree controlled the actions of the board of directors during its negotiation of the merger. Thus, although the Court noted its hesitancy to conclude that the complaint's other allegations could not conceivably state a claim that Oaktree was a controller, the Court ultimately decided that the plaintiffs' complaint (which the Court characterized as supplying "little in the way of specific allegations of control") nevertheless failed to show that Oaktree was conflicted as to the transaction or received some unique benefit from the transaction, and consequently failed to plead that the entire fairness standard applied to the transaction.

In *Sanchez Energy,* the Court examined the controller issue in the context of a derivative action governed by the stricter pleading requirements of Court of Chancery Rule 23.1. The plaintiffs argued that the failure to make a demand on the board of directors of Sanchez Energy Company should be excused because two of the company's co-founders and the collective owners of 21.5% of its stock, A.R. Sanchez Jr. (the company's board chairman) and his son A.R. Sanchez III (the company's chief executive officer), were controlling stockholders who exercised direct managerial control over the company, and the transaction at issue involved another company in which they were investors. While the plaintiffs had alleged that the Sanchezes directed the company's management, the Court found that they did not exercise greater control over the company than that typical of a chief executive officer. Further, citing *KKR Financial* and *Crimson Exploration,* the Court held that, absent particularized allegations that the Sanchezes controlled the decisions of the board of directors with respect to the challenged transaction, the plaintiffs failed to plead sufficiently that the Sanchezes were controlling stockholders under Delaware law.

In contrast to *KKR Financial, Crimson Exploration* and *Sanchez Energy,* the Court in *Zhongpin* denied a motion to dismiss, finding that the plaintiffs had sufficiently

pleaded indicia of domination to raise an inference that Xianfu Zhu, the founder of Zhongpin Inc. ("Zhongpin"), was a controlling stockholder under Delaware law. Zhu held 17.3% of the outstanding voting stock of Zhongpin and was also Zhongpin's chairman of the board and chief executive officer. The plaintiffs, former stockholders of Zhongpin, challenged a going-private transaction in which Zhu acquired all of the company's outstanding stock, alleging that Zhu was a controlling stockholder that stood on both sides of the transaction. Unlike in *Sanchez Energy,* the Court determined that the plaintiffs' allegations (gleaned primarily from the company's own disclosures in a Form 10-K filed with the Securities and Exchange Commission) supported an inference that Zhu exercised significantly more power over Zhongpin than would be expected of a chief executive officer and 17% stockholder. In addition to crediting the plaintiffs' argument that the alleged controller possessed active control over Zhongpin's day-to-day operations, the Court found that the complaint raised an inference that Zhu possessed latent control over Zhongpin through his stock ownership. The Court noted that disclosure in the company's 10-K cited by the plaintiffs implied that Zhu could exercise significant influence over stockholder approvals for the election of directors, mergers and acquisitions, and amendments to the company's bylaws.

In addition, in *Zhongpin* and another controlling stockholder case recently decided by the Court, *In re Cornerstone Therapeutics Inc. Stockholder Litigation,* 2014 WL 4418169 (Del. Ch. Sept. 10, 2014), a separate issue arose as to whether, assuming entire fairness review applied to claims against a controlling stockholder, claims against the disinterested directors could nevertheless be dismissed at the pleading stage because they were exculpated from personal liability under a company's certificate of incorporation. The disinterested directors in both cases argued that in the absence of any allegations raising an inference that they breached any non-exculpated duty, the exculpation provision in the company's certificate of incorporation mandated dismissal even if the Court concluded that entire fairness was the operative standard of review. In both *Cornerstone* and *Zhongpin,* the Court held that, despite the persuasive force of the argument, precedent directs that the Court must await a developed post-trial record before determining the liability of the directors.

In re KKR Financial Holdings LLC Shareholder Litigation, 101 A.3d 980 (Del. Ch. 2014).

In *In re KKR Financial Holdings LLC Shareholder Litigation*, 101 A.3d 980 (Del. Ch. 2014), the Court of Chancery granted the defendants' motions to dismiss with prejudice a suit challenging the acquisition of KKR Financial Holdings LLC ("KFN") by KKR & Co. L.P. ("KKR").

In December 2013, KKR and KFN executed a stock-for-stock merger agreement, which was subject to approval by a majority of KFN shares held by persons other than KKR and its affiliates. The merger was approved on April 30, 2014, by the requisite majority vote.

Nine lawsuits challenging the merger were brought in the Court of Chancery and consolidated. The operative complaint alleged that the members of the KFN board breached their fiduciary duties by agreeing to the merger, that KKR breached its fiduciary duty as a controlling stockholder by causing KFN to enter into the merger agreement, and that KKR and its subsidiaries aided and abetted the KFN board's breach of fiduciary duty.

The Court ruled that KKR, which owned less than 1% of KFN's stock, was not a controlling stockholder. The plaintiffs focused on a management agreement by which a KKR affiliate managed the day-to-day business of KFN, but the Court ruled that the plaintiffs' allegations were not sufficient to support an inference that KKR thereby controlled the KFN board "such that the KFN directors could not freely exercise their judgment in determining whether or not to approve and recommend to the stockholders a merger with KKR." Therefore, the Court dismissed the claim premised on KKR's status as an alleged controlling stockholder.

The Court then held that business judgment review applied to the merger because a majority of the KFN board was disinterested and independent. The

Court held alternatively that, even if a majority of the KFN directors were not independent, "the business judgment presumption still would apply because of the effect of untainted stockholder approval of the merger." The Court rejected the plaintiffs' disclosure challenges and ruled that the business judgment standard of review would apply to the merger "because it was approved by a majority of the shares held by disinterested stockholders of KFN in a vote that was fully informed." Accordingly, the Court dismissed the claim against the KFN directors. Because the plaintiffs had not pleaded a viable claim against the KFN directors, the Court also dismissed the claim for aiding and abetting.

Kahn, et al. v. M&F Worldwide Corp., et al., 88 A.3d 635 (Del. 2014).

In *Kahn, et al. v. M&F Worldwide Corp., et al.,* 88 A.3d 635 (Del. 2014), the Delaware Supreme Court affirmed the Court of Chancery's decision in *In re MFW Shareholders Litigation,* 67 A.3d 496 (Del. Ch. 2013), which granted summary judgment in favor of a board accused of breaching its fiduciary duties by approving a buyout by a 43.4% controlling stockholder, where the controller committed in its initial proposal not to move forward with a transaction unless approved by a special committee, and further committed that any transaction would be subject to a non-waivable condition requiring the approval of the holders of a majority of the shares not owned by the controller and its affiliates. The stockholder plaintiffs initially sought to enjoin the proposed transaction, but withdrew their preliminary injunction application and instead sought post-closing damage relief. After extensive discovery, the defendants sought summary judgment.

The Court of Chancery held that the transaction could be reviewed under the business judgment standard, rather than entire fairness, and granted the defendants' motion. On appeal, the Supreme Court affirmed the Court of Chancery's decision and adopted its formulation of the standard, holding that the business judgment standard of review will be applied in controller buyouts if and only if: (i) the controller conditions the procession of the transaction on the approval of both a special committee and a majority of the minority stockholders; (ii) the special committee is independent; (iii) the special committee is empowered to freely select its own advisors and to say no definitively; (iv) the special committee meets its duty of care in negotiating a fair price; (v) the minority vote is informed; and (vi) there is no coercion of the minority.

The Court further held, however, that if "after discovery triable issues of fact remain about whether either or both of the dual procedural protections were established, or if established were effective, the case will proceed to a trial in which the court will conduct an entire fairness review." The Court also noted that the complaint in the action would have survived a motion to dismiss based on allegations attacking the fairness of the price, which called into question the adequacy of the special committee's negotiations, thereby necessitating discovery on all of the prerequisites to the application of the business judgment rule. ■

ESG Capital Partners II, LP v. Passport Special Opportunities Master Fund, LP, 2015 WL 9060982 (Del. Ch. Dec. 16, 2015).

In a recent opinion, the Delaware Court of Chancery considered, among other things, the impact of an integration clause contained in a subscription agreement for interests in a Delaware limited partnership on a side letter between the limited partnership and an investor, as well as the authority of a general partner to cause the limited partnership to enter into such a side letter. On the facts of this case, the Court found that the subscription agreement's integration clause rendered the side letter a nullity and that the general partner did not have the authority to grant certain rights purported to be provided in the side letter.

In *ESG Capital Partners II, LP v. Passport Special Opportunities Master Fund, LP,* C.A. No. 11053-VCL (Del. Ch. Dec. 16, 2015), Timothy Burns formed ESG Capital Partners II, LP, a Delaware limited partnership (the "Partnership"), for the limited purpose of raising money from investors to purchase shares of Facebook stock before its anticipated IPO. Following the IPO, it was anticipated that the Partnership would then distribute to its investors the Facebook shares or their equivalent cash value, as stipulated in the Partnership's partnership agreement. The partnership agreement gave each of the investors an equity stake in the Partnership and provided that any distribution was to be made to all of the investors in proportion to their respective percentage interests in the Partnership. Following Facebook's IPO, Mr. Burns wrongfully diverted cash, shares and other Partnership property and, before his wrongdoing was discovered, made preferential transfers of Facebook stock to certain limited partners of the Partnership (the "Favored LPs") instead of complying with the distribution provisions set out in the partnership agreement. The Favored LPs received one Facebook share for each of their Partnership units without regard to their actual percentage interests in the Partnership. As a result of Mr. Burns' wrongful actions, the other limited partners

of the Partnership (the "Disfavored LPs") either did not receive any Facebook shares or received less than one Facebook share for each of their Partnership units. Mr. Burns was subsequently indicted criminally and convicted for his misconduct. The Disfavored LPs sued the Favored LPs, asserting that the Favored LPs had breached the partnership agreement by receiving the excess Facebook shares, had wrongfully converted property, and were unjustly enriched.

In connection with a motion to dismiss, the Court denied the Favored LPs' primary defense that they held an ownership interest in the Partnership's Facebook shares and, therefore, did not breach the distribution provisions of the partnership agreement because they were entitled to receive a number of Facebook shares equal to the number of units they held in the Partnership. The Court struck down this argument, finding that it was contrary to (i) the Delaware Revised Uniform Limited Partnership Act (the "LP Act"), which provides that a partnership is a separate legal entity and the individual partners of a partnership do not have any rights in specific partnership property but instead have an interest in the profits and losses of the partnership; and (ii) the plain language of the partnership agreement, which contemplated distributions being made to all of the partners as a class in accordance with their respective percentage interests in the Partnership and not as one-off preferential transfers to certain limited partners.

The Court further disagreed with the Favored LPs' proposition that the sole means for challenging any Partnership distribution was through Section 17-607(b) of the LP Act, and because the Disfavored LPs did not use this means, their claim should be dismissed. The Court held that what occurred was not a distribution, but was in fact a preferential transfer to the Favored LPs. Additionally, the Court held that Section 17-607(b) of the LP Act is not the exclusive means of challenging a distribution, as such provision does not contain any text implying exclusivity. The Court concluded that while Section 17-607 of the LP Act does impose a limitation on distributions, it is not the exclusive limitation, and here it was not an applicable limitation with respect to the preferential transfer made to the Favored LPs.

Of particular interest to practitioners and investors who deal with side letters is the Court's examination and analysis of a side letter (the "Side Letter") that was entered into between the Partnership and one of the Favored LPs. The Side Letter purported to provide a Favored LP with certain preferential rights not provided to other limited partners, including a provision that such Favored LP "held" a specific number of Facebook shares. The Court rejected the argument that the preferential transfer of Facebook shares to the Favored LP was protected because of the specific rights provided under the Side Letter. The Court held that the Side Letter was rendered a nullity because of the integration clause in the Favored LP's subscription agreement that was entered into after the Favored LP entered into the Side Letter. The Court further concluded that even if the Side Letter remained in effect notwithstanding the integration clause contained in the subscription agreement, the Side Letter rights at issue were not valid because (i) the general partner of the Partnership lacked the authority to grant such rights, and the Favored LP knew about such limitation on the general partner's authority; and (ii) the Side Letter could not be used as a means to amend the partnership agreement without complying with the partnership agreement's amendment provisions.

Side letter agreements are regularly used as a means of interpreting, establishing rights under, altering or supplementing the terms contained in partnership agreements and subscription agreements. Practitioners and investors who deal with side letters should give careful consideration to the Court's side letter analysis and whether side letters being entered into in particular transactions are permitted to grant the applicable rights under applicable governing documents and are consistent with relevant integration clauses.

In re Kinder Morgan, Inc. Corporate Reorganization Litigation, 2015 WL 4975270 (Del. Ch. Aug. 20, 2015).

The Delaware courts have consistently held, in the context of Delaware limited partnerships, that clear, express and unambiguous language modifying default fiduciary duties will be enforced. Given this precedent,

the Court of Chancery's decision four months ago in *In re El Paso Pipeline Partners, L.P. Derivative Litigation,* C.A. No. 7141-VCL (Del. Ch. Apr. 20, 2015), in which the Court awarded damages against the general partner of a master limited partnership ("MLP") in connection with a conflict of interest transaction, received significant attention. The Court's very recent decision in *In re Kinder Morgan, Inc. Corporate Reorganization Litigation,* C.A. No. 10093-VCL (Del. Ch. Aug. 20, 2015), confirms that the Delaware courts will continue to enforce the language of partnership agreements (and modifications of fiduciary duty in partnership agreements) as written.

Kinder Morgan involved a corporate reorganization in which Kinder Morgan, Inc. ("Parent") would emerge as the only publicly traded entity and, among other things, two previously publicly traded entities controlled by Parent—Kinder Morgan Energy Partners, L.P. (the "Partnership") and Kinder Morgan Management, LLC ("GP Delegate")—would become wholly owned indirect subsidiaries of Parent. The acquisition of the Partnership was approved by a conflicts committee at the general partner of the Partnership, and the acquisition of the GP Delegate was approved by a conflicts committee at the general partner of the GP Delegate. Both of these conflicts committees consisted of the same three individuals. The plaintiffs alleged, among other things, that the committee did not act in good faith. They claimed that, had the committee acted in good faith, it would have refused to approve Parent's acquisition of the Partnership and, if there were to be a transaction, would have extracted greater consideration from Parent and greater consideration relative to what was paid to acquire GP Delegate.

The Court ruled that based on the language of the Partnership's partnership agreement and Delaware Supreme Court precedent interpreting identical language, all default fiduciary duties had been eliminated and replaced by a contractual obligation for the general partner to act in manner that it "reasonably believed…to be in, or not inconsistent with, the best interests of the Partnership." Therefore, there could be no breach of fiduciary duty claim. Turning to the language of the partnership agreement, the Court held that the relevant standard required that the conflicts committee consider and make a determination as to the fairness of the transaction to, and the best interests of, the Partnership itself as opposed to the limited partners of the Partnership. Notably, the Court stated that if the partnership agreement had required the conflicts committee to make a determination as to the best interests of the limited partners, then the complaint would have been sufficient to withstand a motion to dismiss. Nevertheless, given that the standards in the partnership agreement were based on the interests of the Partnership, the Court applied the standards as written and dismissed the plaintiffs' claims.

The *Kinder Morgan* decision further confirms the contractual flexibility with Delaware limited partnerships and that Delaware courts will enforce clear, express and unambiguous language modifying default fiduciary duties. As the *El Paso* decision demonstrated, however, care should be taken in structuring transactions and the process to comply with the contractual standards established by a partnership agreement.

In re El Paso Pipeline Partners, L.P. Derivative Litigation, 2015 WL 1815846 (Del. Ch. Apr. 20, 2015).

While Delaware courts have consistently held that clear, express and unambiguous language modifying default fiduciary duties will be enforced, the post-trial decision in *In re El Paso Pipeline Partners, L.P. Derivative Litigation,* C.A. No. 7141-VCL (Del. Ch. Apr. 20, 2015), demonstrates that even where default fiduciary duties have been modified or eliminated, a conflict of interest transaction may still run afoul of the contractual standards set forth in a partnership agreement.

In *El Paso,* the transaction at issue was the second of two so-called dropdown transactions by which El Paso Pipeline Partners, L.P. ("El Paso MLP") acquired all of the business involving the liquefied natural gas terminal on Elba Island, Georgia, from El Paso Corporation ("Parent"). Parent owned the general partner of El Paso MLP, and thus controlled El Paso MLP. El Paso MLP's partnership agreement eliminated default fiduciary duties and replaced them with a contractual standard requiring that the persons approving an action on behalf of El Paso MLP subjectively believe that the action is in

the best interests of El Paso MLP. Here, the conflicts committee responsible for approving the dropdown transaction was composed solely of independent directors, had engaged its own legal and financial advisors, had received from its financial advisor an opinion that the challenged transaction was fair from a financial point of view to the unaffiliated unitholders of El Paso MLP, and ultimately approved the transaction.

The Court ruled that under El Paso MLP's partnership agreement each conflicts committee member had an affirmative duty to conclude that the challenged transaction was "in the best interests of [El Paso MLP]." The Court found several flaws with the conflicts committee's process and the valuation analysis. More significantly, the Court found that, despite trial testimony to the contrary, the conflicts committee members did not actually conclude that the challenged transaction was in the best interests of El Paso MLP. The Court found that the conflicts committee had focused extensively on the expected accretion from the challenged transaction—*i.e.,* the amount by which the cash distributions for common unitholders of El Paso MLP would be expected to increase—but failed to take sufficiently into account the valuation of the assets being acquired under traditional valuation analyses. As a result of these findings, the Court awarded damages of $171 million, which the Court determined to be the difference between what El Paso MLP actually paid for the assets acquired in the challenged transaction and the fair value of the assets. Notably, only the general partner entity was held liable for the award, as none of the other defendants was a party to the partnership agreement and the plaintiff did not present a meaningful theory of secondary liability.

The *El Paso* decision is a reminder that, although contractual flexibility afforded to Delaware limited partnerships can be used to provide general partners with significant protections, there is still room for courts to scrutinize compliance with contractual standards.

Allen v. Encore Energy Partners, L.P., 72 A.2d 93 (Del. 2013).

In the latest of a series of decisions addressing conflict of interest transactions involving Delaware limited partnerships, the Delaware Supreme Court once again confirmed that clear, express and unambiguous language modifying default fiduciary duties will be enforced. The transaction at issue in *Allen v. Encore Energy Partners,* L.P., No. 534, 2012 (Del. July 22, 2013), was a merger of a publicly traded Delaware limited partnership with its general partner's controller. The plaintiff was a limited partner of Encore who alleged that the general partner, its controller, and its directors breached the contractual duties imposed by the limited partnership agreement in connection with the merger. The Court of Chancery dismissed the complaint, and the Delaware Supreme Court affirmed such dismissal upon appeal by the plaintiff.

The Supreme Court noted that the limited partnership agreement replaced default fiduciary duties with a contractual duty that would be satisfied if the transaction at issue was approved in "good faith" (as defined by the limited partnership agreement) by the conflicts committee of the board of directors of the general partner. The Supreme Court concluded that the contractual "good faith" standard under the Encore limited partnership agreement requires a subjective belief that the determination or other action is in the best interests of Encore. Thus, for the plaintiff to meet his pleading burden, he would have to adequately plead either that (i) the conflicts committee believed it was acting against Encore's best interests when approving the merger, or (ii) the conflicts committee consciously disregarded its duty to form a subjective belief that the merger was in Encore's best interests. As the Supreme Court observed, it would likely take an extraordinary set of facts to meet such a pleading burden, and the plaintiff failed to do so here.

The *Allen v. Encore Energy* decision is yet another example that Delaware courts will not import standards of conduct from corporate or tort law where a limited partnership agreement effectively modifies default duties and establishes clear contractual standards. The contractual flexibility afforded to Delaware limited partnerships can be used to provide general partners with significant protections. ■

2015 Amendments to the Delaware General Corporation Law

Senate Bill 75, which contains several important amendments to the General Corporation Law of the State of Delaware (the "DGCL"), was signed by Delaware Governor Jack Markell on June 24, 2015. The amendments (other than the amendments to Section 204, Section 205 and Section 363(b)) became effective on August 1, 2015. The amendments to Sections 204 and 205 apply to resolutions adopted by the board ratifying defective corporate acts or stock on or after August 1, 2015. The amendments to Section 363(b) apply to agreements of merger or consolidation entered into on or after August 1, 2015 and to amendments to the certificate of incorporation approved by the board of directors on or after August 1, 2015. The 2015 amendments to the DGCL effect, among others, the following significant changes.

Prohibition on Fee-Shifting Provisions

The 2015 legislation invalidates so-called fee-shifting provisions in certificates of incorporation and bylaws of stock corporations. The legislation was proposed in response to the Delaware Supreme Court's ruling in *ATP Tour, Inc. v. Deutscher Tennis Bund,* 91 A.3d 554 (Del. 2014). In *ATP,* the Court held that a bylaw that made the members of a nonstock corporation liable for the corporation's legal expenses in certain intra-corporate disputes was facially valid—which is to say that, without regard to equitable considerations surrounding its adoption or use, the bylaw was not in contravention of law. The new legislation limits the *ATP* Court's ruling to nonstock corporations.

To accomplish the foregoing, the legislation adds new Section 102(f) to the DGCL. The new subsection provides that a certificate of incorporation may not contain any provision imposing liability on a stockholder for the attorneys' fees or expenses of the corporation or any other party in connection with an "internal corporate claim," as defined in new Section 115 (discussed below). The legislation adds a similar restriction on fee-shifting

provisions to Section 109(b) of the DGCL, which deals with the provisions that may be set forth in the bylaws. The legislation also amends Section 114 to provide that the restrictions on fee-shifting provisions do not apply to nonstock corporations.

Although it invalidates fee-shifting provisions in certificates of incorporation and bylaws of stock corporations, the legislation does not prevent the imposition of such provisions pursuant to any writing signed by a stockholder against whom the provision is to be enforced. Thus, corporations may continue to negotiate for fee-shifting provisions with one or more stockholders in private arrangements, including stock purchase agreements or stockholders' agreements.

Forum-Selection Provisions

The 2015 legislation adds new Section 115 to the DGCL, authorizing the certificate of incorporation or bylaws to include forum-selection provisions. Consistent with the Delaware Court of Chancery's holding in *Boilermakers Local 154 Retirement Fund v. Chevron Corporation,* 73 A.3d 934 (Del. Ch. 2013), Section 115 confirms that the certificate of incorporation or bylaws of the corporation may specify that "internal corporate claims" (*i.e.,* claims, including those brought in the right of the corporation, (i) that are based upon a violation of a duty by a current or former director or officer or stockholder in such capacity, or (ii) as to which the DGCL confers jurisdiction upon the Court of Chancery) must be brought solely and exclusively in the Delaware courts, including the federal court.

New Section 115 does not expressly authorize or prohibit provisions of the certificate of incorporation or bylaws that select a forum other than the Delaware courts as an additional forum in which an internal corporate claim may be brought, but it does invalidate any such provision selecting courts outside of Delaware, or any arbitral forum, to the extent such provision would purport to prohibit litigation of internal corporate claims in the Delaware courts. As with the fee-shifting amendments, however, Section 115 does not prevent the application of a provision selecting a forum other than the Delaware courts pursuant to a stockholders' agreement or other writing signed by the stockholder against whom the provision is to be enforced.

Section 115 is not intended to shield the manner in which a forum-selection provision has been adopted from equitable review, nor is it intended to foreclose judicial review as to whether the terms of any such provision operate reasonably under particular factual circumstances. Moreover, it is not intended to authorize a provision that would purport to foreclose suit in a federal court based on federal jurisdiction, nor is it intended to limit or expand the jurisdiction of the Delaware Court of Chancery or the Delaware Superior Court.

Stock Issuance

The 2015 legislation amends Section 152 of the DGCL to clarify that the board of directors may authorize stock to be issued in one or more transactions in such numbers and at such times as is determined by a person or body other than the board of directors or a committee of the board, so long as the resolution of the board or committee, as applicable, authorizing the issuance fixes the maximum number of shares that may be issued as well as the time frame during which such shares may be issued and establishes a minimum amount of consideration for which such shares may be issued. The minimum amount of consideration cannot be less than the consideration required pursuant to Section 153 of the DGCL, which, as a general matter, means that shares with par value may not be issued for consideration having a value less than the par value of the shares. The legislation clarifies that a formula by which the consideration for stock is determined may include reference to or be made dependent upon the operation of extrinsic facts, thereby confirming that the consideration may be based on, among other things, market prices on one or more dates or averages of market prices on one or more dates. Among other things, the legislation clarifies that the board (or duly empowered committee) may authorize stock to be issued pursuant to "at the market" programs without separately authorizing each individual stock issuance pursuant to the program. In addition, the legislation allows the board to delegate to officers the ability to issue restricted stock on the same basis that the board may delegate to officers the ability to issue rights or options under Section 157(c) of the DGCL.

Consideration for Options and Rights

Consistent with the amendments to Section 152, the 2015 legislation amends Section 157 of the DGCL, which deals with the creation and issuance of rights and options to purchase stock, to clarify that a formula by which the consideration for stock issued upon the exercise of rights and options is determined may include reference to or be made dependent upon the operation of extrinsic facts, such as market prices on one or more dates, or averages of market prices on one or more dates.

Ratification of Defective Corporate Acts

The 2015 legislation makes several amendments to Section 204 of the DGCL, which sets forth the procedures for ratifying stock or corporate acts that, due to a "failure of authorization," would be void or voidable, to clarify and confirm various aspects of its operation, and to provide additional guidance as to the specific requirements for the filing of certificates of validation. The legislation makes conforming amendments to Section 205 of the DGCL, which confers jurisdiction on the Court of Chancery to hear and determine, among other things, the validity of any ratification effected pursuant to Section 204 and the validity of any corporate act or transaction.

Multiple Defective Corporate Acts. The basic premise of Section 204 is that, to ratify a defective corporate act or stock, the board must first take action to effect the ratification. The board's action must then be submitted to stockholders for adoption if the underlying act is one that requires a stockholder vote, or is one that would have required a stockholder vote, either at the time the ratification is submitted for adoption or at the time the original act was taken. Pre-amendment Section 204 requires that the board adopt a "resolution" setting forth, among other things, the defective corporate act being ratified and provides that, where a stockholder vote is or was required, the stockholders must adopt that resolution. As amended, Section 204 dispenses with the notion of the board's ratifying resolution, requiring instead that the board may initiate the ratification process by approving the ratification of one or more defective corporate acts. Under amended Section 204, it is clear that the board may ratify (or initiate the process to ratify) multiple defective corporate acts in a single set of resolutions. Section 204(c), which deals with the circumstances under which a defective corporate act must be approved by stockholders, has been revised to provide that each defective corporate act—rather than the board's resolution ratifying a defective corporate act—that requires or required a vote of stockholders must be submitted to stockholders for their approval.

Ratification of the Failure of the Incorporator to Elect the Initial Board. New Section 204(b)(2) addresses the situation in which the corporation's initial directors have not been (and were not intended to be) elected in the original certificate of incorporation, and the original incorporator never elected the initial directors or evidence of such election cannot be located. Under the new subsection, the corporation's "de facto" directors may adopt a resolution that ratifies the election of those persons who, despite having not been named in the certificate of incorporation or duly elected by the incorporator as the initial directors, first took action on behalf of the corporation as the board of directors. The new subsection does not, by negative implication or otherwise, preclude the filing of a certificate of correction pursuant to Section 103(f) of the DGCL to correct a certificate of incorporation that was intended to (but did not) name the initial directors, nor does it prevent the incorporator from executing (albeit late) an instrument signed in the manner permitted by Section 108 of the DGCL to elect such initial directors.

Stockholder Approval. Section 204, as originally adopted, was intended to provide that only the holders of valid stock would be entitled to vote on any ratifying resolution required to be submitted to stockholders for adoption. Due to the retroactive effect that Section 204 provides to defective corporate acts, some practitioners raised the concern that the ratification of a defective corporate act arguably would cause putative stock that is "outstanding" at the time of the record date for determining stockholders entitled to vote to be retroactively cured such that holders of putative stock would be deemed to be holders of valid stock entitled to vote as of the earlier record date —and their putative shares would be counted in the ratification vote for quorum and voting purposes. As amended, Section 204(d) makes clear that the only

stockholders entitled to vote on the ratification of a defective corporate act, or be counted for purposes of a quorum for such vote, are the holders of record of valid stock as of the record date for determining stockholders entitled to vote thereon. Section 204(f), which provides the retroactive effect to defective corporate acts, has also been amended to clarify the point.

Certificates of Validation. Pre-amendment Section 204 provides that a certificate of validation must be filed with the Delaware Secretary of State whenever the underlying defective corporate act that is being ratified would have required the filing of an instrument under another section of the DGCL. Those certificates of validation must include a copy of the board's resolutions ratifying the defective corporate act as well as the information that would have been required by such other section of the DGCL. Due to the significant variation in defective corporate acts and the resolutions used to ratify them, certificates of validation, unlike most other instruments filed under the DGCL, tend to lack uniformity. As a result, Section 204(e) has been amended to clarify the requirements in respect of certificates of validation, with the ultimate goal of providing greater uniformity.

As amended, Section 204(e) no longer requires that a certificate of validation include a copy of the board's ratifying resolutions and instead provides that the certificate of validation must set forth specified information regarding the defective corporate act and the related failure of authorization. In addition, Section 204(e) requires different types of information to be set forth on or attached to the certificate of validation depending on the history of filings (or lack thereof) with the Delaware Secretary of State in respect of the applicable defective corporate act. The circumstances under which the certificates would vary are as follows:

- Where a certificate in respect of the defective corporate act had previously been filed and no changes are required to give effect to the ratification of such act, Section 204(e) requires the certificate as previously filed with the Delaware Secretary of State to be attached to the certificate of validation as an exhibit.
- Where a certificate in respect of the defective corporate act had previously been filed and changes are required to that certificate to give effect to the ratification of such act, Section 204(e) requires that a certificate containing all of the information required under the other section of the DGCL, including the changes necessary to give effect to the ratification of the defective corporate act, be attached to the certificate of validation as an exhibit. In that case, the certificate of validation must state the date and time as of which the certificate attached to it would have become effective.
- Where no certificate had previously been filed and the filing of a certificate was required to give effect to the ratification of a defective corporate act, Section 204(e) requires that a certificate containing all of the information required under the other section of the DGCL be attached to the certificate of validation as an exhibit. In that case, the certificate of validation must also state the date and time as of which the certificate attached to it would have become effective.

Action by Written Consent and Notice. Section 204, as originally drafted, included concepts relating to the submission of the board's ratifying resolution to stockholders at a duly called and held meeting. As with virtually all other sections of the DGCL, Section 204 did not specifically reference the stockholders' power to act by written consent to approve any ratifying resolution, as it was understood that, pursuant to Section 228 of the DGCL, unless otherwise restricted by the certificate of incorporation, stockholders could act by written consent in lieu of a meeting with respect to any matter required or permitted to be acted upon by stockholders at a meeting. Nevertheless, the procedures for notice in cases where stockholders are acting by written consent in lieu of a meeting were viewed as fairly difficult to parse under existing Section 204. The amendments to Section 204 clarify these procedures.

As amended, Section 204(g) expressly provides that, where the ratification of a defective corporate act is approved by consent of stockholders in lieu of a meeting, the notice required by Section 204(g) may be included in the notice required to be given pursuant to Section 228(e). Section 204(g) now clarifies that, where

a notice sent pursuant to Section 204(g) is included in a notice sent pursuant to Section 228(e), the notice must be sent to the parties entitled to receive the notice under both Section 204(g) and Section 228(e). Section 204(g) further clarifies that no such notice need be provided to any holder of valid shares that acted by written consent in lieu of a meeting to approve the ratification of a defective corporate act or to any holder of putative shares who otherwise consented thereto in writing.

In addition, Section 204(g) provides that corporations that have a class of stock listed on a national securities exchange may give the notice required by Section 204(g) by means of a public filing with the Securities and Exchange Commission.

Validation Effective Time. Prior to the amendment, Section 204(h)(6) defined "validation effective time" as the later of (x) the time at which the ratification of the defective corporate act is approved by stockholders (or, if no vote is required, the time at which the notice required by Section 204(g) is given) and (y) the time at which any certificate of validation has become effective. As amended, Section 204(h)(6) confirms that, in respect of the ratification of any defective corporate act for which the "validation effective time" is the time at which the stockholders approve the ratification of the defective corporate act, such validation effective time occurs at the time of stockholder approval regardless of whether the stockholders are acting at a meeting or by consent in lieu of a meeting pursuant to Section 228. Although the amendment clarifies that, in such cases, the validation effective time commences upon the stockholders' approval of the ratification of the defective corporate act, a corresponding amendment to Section 204(g) confirms that the 120-day period during which stockholders may challenge the ratification of a defective corporate act commences from the later of the validation effective time and the time at which the notice required by Section 204(g) is given. In light of the corresponding amendment to the commencement of the 120-day challenge period in Section 204(g), Section 204(h)(6), as amended, further provides that where the ratification of the defective corporate act does not require stockholder approval or the filing of a certificate of validation, the validation effective time is the time at which the board of directors adopts the resolutions to approve the ratification of the defective corporate act.

The definition of "validation effective time" has also been amended in a manner that permits the board of directors to fix a future validation effective time for any defective corporate act that does not require the filing of a certificate of validation. Where the board of directors fixes a future validation effective time, such validation effective time may not precede the time at which a defective corporate act requiring a vote of stockholders is approved by stockholders. Again, the 120-day period during which challenges to the ratification may be brought would commence from the later of the validation effective time and the time at which the notice required by Section 204(g) is given. The amendments are intended to obviate logistical issues that may arise in connection with the delivery of notices in situations where multiple defective corporate acts are being ratified at the same time. As amended, Section 204(h)(6) enables the board to set one date on which the ratification of all defective corporate acts approved by the board will be effective, regardless of when the notice under Section 204(g) is sent or when each defective corporate act would otherwise become effective under Section 204(h)(6).

120-Day Challenge Period. Consistent with the amendments to Sections 204(g) and 204(h)(6) in respect of the validation effective time and the commencement of the 120-day period during which an action may be brought to challenge the ratification of a defective corporate act, Section 205(f) has been amended to provide that no such action may be brought after the expiration of 120 days from the later of the validation effective time and the time that notice of the ratification is given under Section 204(g), if notice is required to be given under such section.

Restatements of Certificates of Incorporation

In 2014, Section 242 of the DGCL was amended to eliminate the requirement to obtain a stockholder vote on an amendment to the certificate of incorporation to effect a change of the corporation's name. In furtherance of that amendment, Section 245(c) has been amended to clarify that a restated certificate of incorporation need not state that it does not further amend the provisions

of the corporation's certificate of incorporation if the only amendment is to change the corporation's name without a vote of the stockholders.

Corporate Name

The 2015 legislation permits the Division of Corporations of the Delaware Secretary of State (the "Division") to waive, under limited circumstances, the requirement with respect to the use of a name that has been reserved for use with the Division or is on the Division's records. Section 102(a)(1)(ii) of the DGCL provides that a Delaware corporation's name as set forth in its certificate of incorporation shall be such as to distinguish it upon the Division's records from the names that have been reserved for use with the Division and from the names on record with the Division of each other corporation, partnership, limited partnership, limited liability company or statutory trust organized or registered as a domestic or foreign corporation, partnership, limited partnership, limited liability company or statutory trust under the laws of the State of Delaware, except with the written consent of the person who has reserved the name of such corporation, partnership, limited partnership, limited liability company or statutory trust. The 2015 legislation adds a further exception such that, without prejudicing any rights of the person who has reserved the name or of such other corporation, partnership, limited partnership, limited liability company or statutory trust, the Division may waive the requirement if the corporation seeking such waiver demonstrates to the satisfaction of the Delaware Secretary of State that (a) such corporation or a predecessor entity previously has made substantial use of the name or a substantially similar name, (b) such corporation has made reasonable efforts to secure such written consent, and (c) the waiver is in the interest of the State of Delaware.

Public Benefit Corporations

The 2015 legislation makes several changes with respect to the provisions of the DGCL dealing with public benefit corporations. Section 362(c) has been amended to eliminate the requirement that a public benefit corporation include in its name a specific "public benefit corporation" identifier. If the identifier is excluded, however, the corporation must, before issuing or disposing of shares, provide notice to any person acquiring the shares so issued or disposed of that the corporation is a public benefit corporation, unless the issuance is being made pursuant to an offering under the Securities Act of 1933 or the corporation has at the time of issuance a class of stock registered under the Securities Exchange Act of 1934.

The legislation also changes Section 363(a) and Section 363(c) to relax the voting standards required to approve charter amendments or transactions in which a corporation that is not a public benefit corporation becomes a public benefit corporation or its stockholders become stockholders of a public benefit corporation, as well as charter amendments or transactions in which a public benefit corporation ceases to be a public benefit corporation or its stockholders become stockholders of a corporation that is not a public benefit corporation. Prior to the amendments, Sections 363(a) and 363(c) provided that such actions required the approval of 90% of the outstanding shares of each class of stock, whether voting or nonvoting. The new legislation reduces the voting standard on these matters to 66 2/3% of the outstanding shares entitled to vote.

Prior to the 2015 amendments, Section 363(b) provided that stockholders of a corporation that is not a public benefit corporation are entitled to statutory appraisal rights in cases where the corporation amends its certificate of incorporation to become a public benefit corporation or effects a merger or consolidation that results in the shares of its stock becoming, or being converted into the right to receive, shares of a public benefit corporation. The 2015 amendments to Section 363(b) provide a "market out" exception to these rights (similar to the exception that applies to appraisal rights generally under Section 262). Under the amendments, no such appraisal rights are available for shares of stock (or depository receipts in respect thereof) that, at the record date fixed to determine stockholders entitled to receive notice of the meeting of stockholders to act upon any such agreement of merger or consolidation, or to adopt any such amendment, were either listed on a national securities exchange or held of record by more than 2,000 holders, unless, in the case of a merger or consolidation, the holders are required by the terms of the merger to accept anything other

than shares of stock (or depository receipts in respect thereof) that will be listed on a national securities exchange or held of record by more than 2,000 holders, cash in lieu of fractional shares (or fractional depository receipts), or any combination of the foregoing.

The Delaware Rapid Arbitration Act

On April 2, 2015, Delaware Governor Jack Markell signed a highly specialized arbitration statute into law: the Delaware Rapid Arbitration Act (the "DRAA"). The DRAA provides a quick and inexpensive process for starting an arbitration proceeding, accelerates the arbitration itself to ensure a swift resolution, eliminates confirmation proceedings, and allows for challenges directly to the Delaware Supreme Court.

Speed and efficiency are key features of the DRAA. Arbitrations brought under the new statute must be completed within 120 days of the arbitrator accepting appointment. With the unanimous consent of the parties and the arbitrator, that timeline can be extended to 180 days. Arbitrators who do not issue final awards within the prescribed timeframe face reductions in their fees corresponding to the length of the delay in the issuance of the final award.

The new legislation gives broad powers to expert arbitrators. Arbitrability is determined solely by the arbitrator, who also has the authority to grant a full array of injunctive and other remedies. The arbitrator's final award is deemed confirmed simply by the passage of time. Challenges to the final award are made directly to the Delaware Supreme Court, skipping review by the trial court. Unless altered by contract, such challenges proceed under the narrow Federal Arbitration Act standard of review.

The DRAA was designed to address resolution of disputes where sophisticated parties most need no-nonsense, swift resolution. The DRAA may not be used to resolve disputes involving consumers, and it may only be invoked against parties who sign an express agreement to arbitrate under the DRAA. One of the parties must be a Delaware business entity, although it need not be located in Delaware.

The DRAA was developed by an interdisciplinary team of arbitration practitioners led by Delaware's Chief Justice Leo E. Strine Jr., Delaware's Chancellor Andre G. Bouchard, and Delaware's Secretary of State Jeffrey Bullock. Richards, Layton & Finger lawyers also played key roles in developing the DRAA: two of our partners were deeply involved in drafting the statute, and a third played a principal role in drafting the proposed model rules.

2015 Amendments to Delaware Alternative Entity Law

Delaware has recently adopted legislation amending the Delaware Limited Liability Company Act (LLC Act), the Delaware Revised Uniform Limited Partnership Act (LP Act) and the Delaware Revised Uniform Partnership Act (GP Act) (collectively, the LLC and Partnership Acts). The following is a brief summary of some of the more significant amendments that affect Delaware limited liability companies (Delaware LLCs), Delaware limited partnerships (Delaware LPs) and Delaware general partnerships (Delaware GPs).

Default Class or Group Voting Requirements Eliminated

The LLC Act and the LP Act have been amended to eliminate the default class or group voting requirements in connection with the merger or consolidation, transfer or continuance, conversion, dissolution and winding up of a Delaware LLC or Delaware LP and the termination and winding up of a series of a Delaware LLC or Delaware LP. The recent amendments provide that, in connection with the foregoing matters, the default class or group voting requirements under the LLC Act and the LP Act, as in effect on July 31, 2015, will continue to apply to a Delaware LLC or Delaware LP whose original certificate of formation or certificate of limited partnership was filed with the Delaware Secretary of

State and is effective on or before July 31, 2015, unless otherwise provided in a limited liability company agreement or partnership agreement.

Additionally, the LP Act has been amended to eliminate the default class or group voting requirements in connection with the revocation of dissolution of a Delaware LP and the conversion of a Delaware LP to a Delaware limited liability limited partnership and to eliminate the default class or group requirement for executing a certificate of cancellation for a Delaware LP that is being wound up by its limited partners. Such default class or group voting and execution requirements were eliminated by the amendments regardless of when an original certificate of limited partnership was filed and effective, unless otherwise provided in a partnership agreement.

In those circumstances in which the default class or group voting and execution requirements have been eliminated by the amendments, the LLC Act and the LP Act will continue to have default voting and execution requirements. However, as a result of the amendments, such default voting and execution requirements will no longer require a class or group vote or, as applicable, execution, in connection with such actions.

Irrevocable Delegation

The LLC and Partnership Acts have been amended to confirm that, unless otherwise provided in a limited liability company agreement or partnership agreement, a delegation of the rights and powers to manage and control the business and affairs of a Delaware LLC, Delaware LP or Delaware GP by a member or manager of a Delaware LLC, a general partner of a Delaware LP or a partner of a Delaware GP shall be irrevocable if such delegation states that it is irrevocable.

Irrevocable Proxy

In 2010, the LLC and Partnership Acts were amended to clarify when a power of attorney will be irrevocable and the effects of such irrevocability for purposes of the laws of the State of Delaware. The recent amendments to the LLC and Partnership Acts confirm that the provisions of the LLC and Partnership Acts relating to irrevocable powers of attorney also apply to proxies and clarify when a proxy will be irrevocable and the effects of such irrevocability for purposes of the laws of the State of Delaware. The LLC and Partnership Acts have also been amended to confirm that the provisions of the LLC and Partnership Acts addressing powers of attorney and proxies will not be construed to limit the enforceability of a power of attorney or proxy that is part of a limited liability company agreement or a partnership agreement.

The recent amendments reflect Delaware's continuing commitment to maintaining statutes governing Delaware LLCs, Delaware LPs and Delaware GPs that effectively serve the business needs of the national and international business communities. The recent amendments to the LLC Act, LP Act and GP Act are contained in Senate Bill Nos. 78, 77 and 76, respectively (each effective August 1, 2015, except that the amendments to Section 18-1105(a)(5) of the LLC Act, Section 17-1107(a)(5) of the LP Act and Section 15-1207(a)(5) of the GP Act, which confirm that the Delaware Secretary of State may issue public records in the form of photocopies or electronic image copies and need not provide public records in any other form, are effective upon their respective enactments into law). ■

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