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CORPORATE GOVERNANCE

2016 Proposed Amendments to the General Corporation Law of the State of Delaware

Anticipated legislation would amend the Delaware General Corporation Law to clarify the requirements and procedures relating to intermediate-form mergers and to address appraisal claims. In addition, it would make technical changes to requirements for board committee and stock certificates.

By John Mark Zeberkiewicz and Brigitte V. Fresco

Legislation setting forth the 2016 proposed amendments to the General Corporation Law of the State of Delaware (DGCL) has been approved by the Corporation Law Section of the Delaware State Bar Association and is expected to be introduced to the Delaware General Assembly. If the amendments become effective, they would result in several important changes to the DGCL. Among other things, the proposed amendments would clarify the requirements and procedures relating to so-called "intermediate-form" mergers under Section 251(h) of the DGCL and would make several changes to Section 262 of the DGCL, which governs appraisal rights, to dispense with certain *de minimis* appraisal claims and to give parties an opportunity to make pre-judgment payments to appraisal claimants to limit the amount of interest that would otherwise accrue on an appraisal award.

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Section 251(h)—Intermediate-Form Mergers

In 2013, the DGCL was amended to eliminate, subject to certain conditions, the need for a back-end merger vote in a two-step merger involving a front-end tender or exchange offer. Since its adoption, Section 251(h) has become a preferred method of accomplishing a tender offer in public M&A transactions. The proposed amendments to Section 251(h) are designed largely to clarify the procedures and requirements of the subsection.

Eligibility to Use Section 251(h); Offers for Different Classes or Series of Stock

Section 251(h) originally was drafted to make the "intermediate-form" merger available principally to public companies. To that end, Section 251(h) currently provides that, unless expressly

required by the certificate of incorporation, no vote of stockholders of a target corporation whose shares are listed on a national securities exchange or held of record by more than 2,000 holders immediately prior to the execution of the merger agreement is required to authorize the merger, so long as the other requirements of the subsection are satisfied.

The proposed amendments to Section 251(h) clarify that the subsection applies to a target corporation that has *any* class or series of stock listed on a national securities exchange or held of record by more than 2,000 holders immediately prior to the execution of the merger agreement—and that not all classes or series of stock need be so listed or held. Thus, a target corporation whose common stock is listed on a national securities exchange may take advantage of Section 251(h), even if it has a series of preferred stock that is not listed or held of record by more than 2,000 holders. The proposed amendments also would clarify that the offer for the stock of the target corporation contemplated by the subsection (the Offer) may be effected through separate offers for separate classes or series of stock.

Additional Minimum Conditions

The proposed amendments would clarify that that the Offer may be conditioned on the tender of a minimum number or percentage of the shares of the stock of the constituent corporation or of any class or series thereof.

Rollover Stock

One of the current requirements of accomplishing a merger under Section 251(h) is that, following the consummation of the Offer, the stock irrevocably accepted for purchase or exchange and received by the depositary, plus the stock otherwise owned by the offeror, equals the percentage of stock, and of each class and series thereof, that would otherwise be required to adopt the merger agreement. The proposed amendments would permit, for purposes of determining whether such requirement has been met, the inclusion of shares of stock of the target held by any person that owns, directly or indirectly, all of the outstanding stock of the offeror, or that is a direct or indirect wholly-owned subsidiary of such person or persons or of the offeror (collectively offeror affiliates). The proposed amendments also would provide that shares of stock of the target corporation that are the subject of a written agreement requiring such shares to be transferred, contributed or delivered to the offeror or any offeror affiliate in exchange for stock or other equity interests in the offeror or any offeror affiliate may be counted for purposes of determining whether the minimum condition required by the statute has been met, so long as such shares are in fact so transferred, contributed or delivered before the effective time of the merger (rollover stock).

The proposed amendments would further provide that rollover stock and shares of the target corporation held in treasury, by any direct or indirect wholly-owned subsidiary of the target, or by the offeror affiliates are excluded from the requirement that they be converted in the merger into, or into the right to receive, the same consideration paid in the Offer. In this manner, the proposed amendments would provide a more direct and efficient means of enabling certain target stockholders to "rollover" their shares in the transaction.

Receipt of Stock

The proposed amendments would clarify the means by which shares of stock of the target corporation are "received" for purposes of determining whether the minimum tender condition required by the subsection has been satisfied. The proposed amendments would clarify that shares represented by certificates will be "received" upon physical receipt of the certificate, together with an executed letter of transmittal, so long as the certificate representing such shares was not cancelled prior to consummation of the Offer.

Under the proposed amendments, uncertificated shares held of record by a clearing corporation as nominee would be "received" by transfer into the depository's account by means of an agent's

message, and all other uncertificated shares would be "received" by physical receipt of an executed letter of transmittal by the depository. In all cases, however, under the proposed amendments, uncertificated shares would cease to be "received" to the extent they have been reduced or eliminated due to any sale of such shares prior to the consummation of the Offer. The proposed amendments would prescribe what constitutes an "agent's message" for these purposes, specifying that it is a message transmitted by the clearing corporation acting as nominee, received by the depository, and forming part of the book-entry confirmation, which states that the clearing corporation has received an express acknowledgment from a stockholder that such stockholder has received the Offer and agrees to be bound by the terms of the Offer, and that the offeror may enforce such agreement against such stockholder.

Section 262—Appraisal Rights

Section 262 of the DGCL, governing appraisal rights, would be amended in two principal respects. First, the proposed amendments would seek to limit *de minimis* appraisal claims in certain transactions involving stock listed on a national securities exchange. Second, the proposed amendments would give surviving corporations the option to pay each stockholder entitled to appraisal at an earlier stage of the appraisal proceeding as a means of cutting off the accrual of interest under the statute with respect to the amount paid.

De Minimis Exception

To implement the first of these changes, the proposed amendments would provide that, if immediately before the merger or consolidation the shares of the class or series of stock of the constituent corporation as to which appraisal rights are available were listed on a national securities exchange, the Court of Chancery of the State of Delaware shall dismiss an appraisal proceeding as to all stockholders otherwise entitled to appraisal rights, unless: (1) the total number of shares entitled to appraisal exceeds 1 percent of the outstanding number of shares of the class or series entitled to appraisal; or (2) the value of the consideration for such total number of shares exceeds $1 million; or (3) the merger was effected as a "short-form" merger under Section 253 or Section 267 of the DGCL.

The amendment is designed to mitigate the risk that a plaintiff will use the appraisal process solely to gain leverage in a settlement negotiation. That is, the amendment is designed to prevent stockholders from demanding an appraisal in cases where the number of shares (or the value of those shares) is minimal, but the surviving corporation may be inclined to settle the claim to avoid the litigation costs attendant to the appraisal proceeding.

It is important to note, however, that if one of those three elements is present, the appraisal rights otherwise available will continue to apply. For example, if the total number of shares entitled to appraisal is less than 1 percent of the outstanding shares of the class or series entitled to appraisal, but the value of the consideration for such shares exceeds $1 million, then the appraisal rights otherwise available will remain. In addition, even if the number of shares entitled to appraisal is less than 1 percent of the outstanding shares of the class or series entitled to appraisal and the consideration for such shares is less than $1 million, the appraisal rights available in a "short-form" merger will continue to apply, as the amendments recognize that appraisal may be the stockholders' only remedy in such a merger. In addition, as indicated above, in no case will the *de minimis* exceptions apply to shares of any class or series of stock of a constituent corporation that were not, immediately before the merger, listed on a national securities exchange.

In connection with the foregoing changes, the proposed amendments also would provide that, where the corporation has adopted a provision in its certificate of incorporation pursuant to Section 262(c) of the DGCL granting appraisal rights in circumstances where they would not otherwise exist (*e.g.*, in connection with amendments to the certificate of incorporation or sales of all or substantially

all of the corporation's assets), an appraisal proceeding brought thereunder will be dismissed if the *de minimis* carve-out would apply.

Tender of Payment

To implement the second of the principal changes to Section 262, the proposed amendments would modify Section 262(h) to provide corporations the option of limiting the accrual of statutory interest on appraisal awards by making an early payment to the appraisal claimants. Section 262(h) currently provides that, unless the Court of Chancery determines otherwise for good cause shown, interest on the amount that is determined to be the "fair value" of appraisal shares will accrue from the effective date of the merger through the date of payment of judgment, will be compounded quarterly, and will accrue at 5 percent over the Federal Reserve discount rate (including any surcharge) as established from time to time during that period. Since payment of "fair value" in an appraisal proceeding is not made until such amount is determined after trial, interest accrues on the full amount of the award, even if the fair value is ultimately determined to be the same as or less than the consideration paid in the merger. The proposed amendments would permit the surviving corporation to pay the appraisal claimants, at any time before the entry of judgment in the proceeding, a sum of money that it determines to be appropriate.

After making the payment, interest would only accrue upon the sum of (1) the difference, if any, between the amount so paid and the fair value of the shares as determined by the Court of Chancery, and (2) interest theretofore accrued, unless paid at that time. Any surviving corporation electing to make such a payment would be required to make the payment to all of the appraisal claimants, unless the surviving corporation has a good faith basis for contesting a particular claimant's entitlement to an appraisal of such claimant's shares, in which case the surviving corporation may elect to make payment only to those stockholders whose entitlement to appraisal is uncontested. The amount that the surviving corporation pays would not give rise to any inference as to the fair value of the shares as to which an appraisal is sought.

Section 111—Jurisdiction

Section 111(a) of the DGCL generally provides that any civil action to interpret, apply, enforce or determine the validity of provisions of various documents, agreements and instruments may be brought in the Court of Chancery, except to the extent that a statute confers exclusive jurisdiction on a court, agency or tribunal other than the Court of Chancery. Section 111(a)(2) of the DGCL currently confers such jurisdiction with respect to any instrument, document or agreement by which a corporation creates or sells, or offers to create or sell, any of its stock, or any rights or options respecting its stock. The proposed amendments would modify Section 111(a)(2) to permit the Court of Chancery to exercise subject matter jurisdiction over civil actions involving certain other instruments, documents, or agreements, including (1) those to which a Delaware corporation is a party and pursuant to which one or more holders of the corporation's stock sell or offer to sell any of such stock, and (2) those by which a Delaware corporation agrees, to sell, lease or exchange any of its property or assets and by which its terms provides that one or more holders of its stock approve or consent to such sale, lease or exchange.

Section 141—Board of Directors and Committees

The proposed amendments would make several technical changes to Section 141 of the DGCL.

Default Quorum and Voting Requirements for Committees and Subcommittees

The proposed amendments would modify Section 141(c) of the DGCL, which deals with the establishment of committees of the board of directors, to specify the default quorum and voting requirements

for committees and subcommittees. Under the proposed amendments, a majority of the directors then serving on a committee or a subcommittee would constitute a quorum (except as otherwise provided in the certificate of incorporation, bylaws, resolutions of the board establishing the committee or resolutions of the committee establishing the subcommittee, provided that in no case may a quorum be less than one-third of the directors serving on the committee or subcommittee). The proposed amendments also would provide that the vote of a majority of the members present at a meeting of the committee or subcommittee at which a quorum is present shall be the act of the committee or subcommittee, unless the certificate of incorporation, the bylaws, the resolutions of the board establishing the committee or the resolutions of the committee establishing the subcommittee require a greater number.

References to Subcommittees

The proposed amendments would clarify that references in the DGCL to board committees (and committee members) will be deemed to include references to subcommittees (and subcommittee members). The proposed amendments would make other conforming changes to Section 141.

Section 158—Stock Certificates

Section 158 of the DGCL currently provides that every holder of stock represented by certificates shall be entitled to have a certificate signed by, or in the name of the corporation by the chairperson or vice-chairperson of the board of directors, or the president or vice-president, and by the treasurer or an assistant treasurer, or the secretary or an assistant secretary of such corporation representing the number of shares registered in certificate form. (It should be noted that Section 142 also requires the corporation to have officers as may be necessary to enable it to sign instruments and stock certificates.) In recent years, many corporations have dispensed with the offices of "President" and "Treasurer" and have assigned the role historically assumed by the President and Treasurer to the Chief Executive Officer and Chief Financial Officer, respectively. In light of developments in practice, the proposed amendment to Section 158 would provide that any two officers of the corporation who are authorized to do so may execute stock certificates on behalf of the corporation. Thus, as a result of the proposed amendments, any two duly empowered officers, regardless of their official title, would be authorized to execute stock certificates. The proposed amendment is not intended to change the existing law that the signatures on a stock certificate may be the signatures of the same person, so long as each signature is made in a separate officer capacity of such person.

Section 311—Restoration

The proposed amendments would modify Section 311 of the DGCL to include a procedure to restore a corporation's certificate of incorporation after it has expired by limitation. This change is consistent with Section 278 of the DGCL, which currently provides that Sections 279 through 282 of the DGCL, relating to corporations that have dissolved, apply to any corporation that has expired by its own limitation. Section 311 also is amended to clarify that a corporation desiring to revoke its dissolution or restore its certificate of incorporation must file all annual franchise tax reports that the corporation would have had to file if it had not dissolved or expired by limitation and pay all franchise taxes that the corporation would have had to pay if it had not dissolved or expired.

Section 312—Revival

The proposed amendments to Section 312 would distinguish the procedure to extend the term of a corporation's certificate of incorporation (which would now solely be governed by Section 242 of the DGCL) or to restore a corporation's certificate of incorporation if it has expired by limitation (which would now be governed by Section 311) from the procedure to revive a corporation's certificate of incorporation

when it has become forfeited, for failing to comply with the provisions of the DGCL relating to registered agents, or void, for failing to file annual franchise tax reports or pay annual franchise taxes. Thus, under the proposed amendments, Section 312 would apply only to a corporation whose certificate of incorporation has become forfeited or void. Accordingly, the proposed amendments would modify Section 312 such that it uses only the term "revival" to reflect the process for reviving such a corporation. (The proposed amendments would eliminate the terms "renewal," "extension" and "restoration.")

The proposed amendments also would clarify and simplify the procedures to be followed by a Delaware corporation to revive its certificate of incorporation after the certificate has become forfeited or void. The amendments clarify that the provisions of Section 312 do not apply to a corporation whose certificate of incorporation has been forfeited or revoked by the Court of Chancery pursuant to Section 284. Of significance, the proposed amendments would provide that a majority of the directors then in office, even if less than a quorum, or the sole director in office, may authorize the revival of the certificate of incorporation. The proposed amendments would identify such directors as those who, but for the certificate of incorporation having become forfeited or void, would be the duly elected or appointed directors of the corporation. In addition, the proposed amendments would clarify the process for elections of directors if no directors are in office and the effect of a revival with respect to actions taken by the corporation's directors, officers, agents and stockholders.

Effective Time of the Amendments

If enacted, the 2016 amendments (other than the amendments to Section 251(h) and Section 262) would become effective on August 1, 2016. The amendments to Section 251(h) would be effective only with respect to merger agreements entered into on or after August 1, 2016. The amendments to Section 262 would be effective only with respect to transactions consummated pursuant to agreements entered into on or after August 1, 2016 (or, in the case of mergers pursuant to Section 253 of the DGCL, resolutions of the board of directors adopted on or after August 1, 2016, or, in the case of mergers pursuant to Section 267 of the DGCL, authorizations provided on or after August 1, 2016).

Conclusion

The 2016 amendments to the DGCL make several important changes, demonstrating Delaware's commitment to reviewing its corporate law regularly to address issues that arise in practice to ensure that its corporate law continues to meet the needs and demands of modern corporate enterprises.