Chancery Court Discusses Continued Viability of *Blasius* Standard

Brock E. Czeschin
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Recently, in *Keyser v. Curtis*, 2012 WL 31154353 (Del. Ch. July 31, 2012), the Court of Chancery applied the entire fairness standard when considering a challenge to the issuance of super-voting preferred stock. Although the preferred stock had been issued as part of an effort to prevent stockholders from electing a new board, Vice Chancellor John W. Noble found that the *Blasius* standard was not applicable. Rather, because the sole director stood on both sides of the preferred stock issuance, the court determined that entire fairness was the applicable standard. The decision provides helpful guidance concerning the continued viability of the *Blasius* standard and how it may be incorporated into Delaware's other standards of review.

The *Keyser* case arose out of a battle for control of Ark Financial Services. Robert D. Keyser was a founder and the former CEO of Ark. When Keyser acquired an option for the purchase of an additional 8 million shares of Ark's common stock, Ark's then-sole director and president, Albert Poliak, realized the exercise of the option would provide Keyser and his allies sufficient shares to change the board. Poliak believed Keyser had proved to be a poor manager in the past and that it was not in the company's best interest for Keyser to regain control of Ark, according to the opinion. In order to prevent Keyser from being able to change the board, Poliak determined to authorize the creation of a new class of Series B preferred stock, which would vote with Ark's common stock as a single class and be entitled to 1,000 votes per share. The Series B preferred stock also had a liquidation preference of $1 per share, redeemable at any time. Poliak determined to issue 25,000 shares of the Series B preferred stock to himself for the price of a penny per share.

As expected, Keyser exercised the option and delivered a written consent purporting to remove Poliak and elect new board members. Poliak disputed the validity and effectiveness of the written consent, in part on the grounds that it was not executed by stockholders with sufficient voting power in light of the Series B preferred stock issuance. Following lengthy efforts to reach a resolution to the parties' disputes, in December 2011, Keyser and his allies delivered another written consent purporting to remove the then-current board and elect a new board. Keyser also initiated litigation in the Court of Chancery seeking a declaration pursuant to Section 225 of the Delaware General Corporation Law that the Series B preferred stock issuance was invalid and that, as a consequence, the written consent was executed by stockholders representing a majority of the company's voting power and was effective in electing the new board.

In considering the proper standard for judging the Series B issuance, the Chancery Court found that Poliak had admitted to causing Ark to make the preferred stock issuance in order to prevent the election of a new board. The court described this purpose as "the quintessential *Blasius* trigger." However, unlike in *Blasius Industries v. Atlas*, 564 A.2d 651 (Del. Ch. 1988) (which involved an expansion of the board in an effort to prevent the election of a new board majority), the *Keyser* case concerned a self-dealing transaction in which Poliak stood on both sides of the deal. For this reason, the Chancery Court concluded that entire fairness, not *Blasius*, was the proper standard of review.

In reaching this decision, the Chancery Court observed that "this court and our Supreme Court have intimated that *Blasius'* main role, to the extent it has one, is a specific iteration of the intermediate standard of review laid out in *Unocal Corp. v. Mesa Petroleum Co.*" The *Keyser* court suggested that this intermediate standard of review should be applied when director self-interest is limited to the desire to remain in office. In circumstances involving more direct forms of self-interest (such as a director granting him or herself preferred stock), the applicable standard should be the more stringent entire fairness test, regardless of the purpose of the transaction. However, just as the *Blasius* standard may be incorporated into intermediate review under *Unocal*, the Chancery Court found that entire fairness review was sufficiently flexible to incorporate the principles of *Blasius* when applied in circumstances involving an effort to impinge on the stockholder franchise. In particular, given the primacy that Delaware law places on the stockholder franchise in the election of directors, the court held that a defendant seeking to establish the entire fairness of a self-dealing transaction that purposely impinged on the franchise would have the burden of showing "a very powerful justification" and "a considerably robust process" for such transaction. Under this formulation of the standard, the court found that Poliak had failed to establish the entire fairness of the Series B preferred stock issuance and that the issuance was therefore invalid.

Accordingly, the *Keyser* decision provides helpful guidance concerning the role of *Blasius* and demonstrates how the principles underlying the *Blasius* decision may be incorporated into the application of the entire fairness or intermediate standards of review when the facts involve action impinging on the stockholder franchise.

Brock E. Czeschin, *a director at Richards, Layton & Finger, represents Delaware corporations and alternative entities, and their directors and managers, in complex litigation matters. He also regularly advises clients with respect to governance and transactional issues relating to Delaware corporations and alternative entities. This article expressed his views and not necessarily those of Richards, Layton or its clients. Czeschin may be reached at czeschin@rlf.com.*