

DELAWARE

Laws & Programs Affecting Business

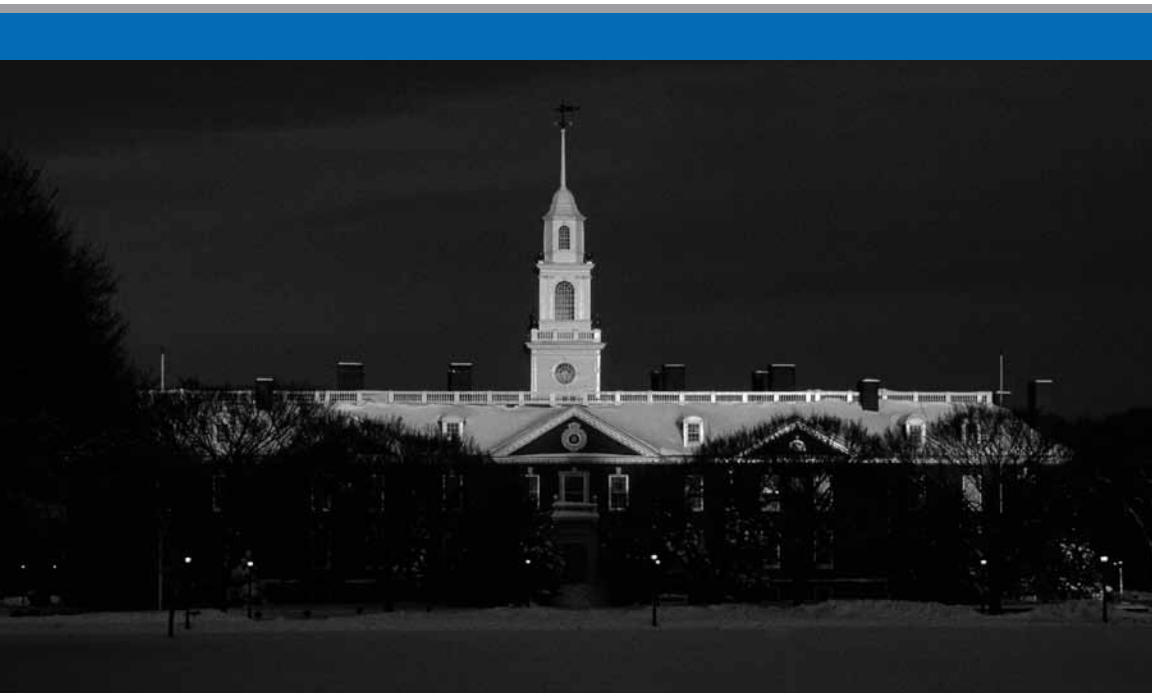


RICHARDS, LAYTON & FINGER



DELAWARE

Laws & Programs Affecting Business



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RICHARDS, LAYTON & FINGER

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The colonial style of Delaware's Legislative Hall, depicted on the front cover, reflects the stability of Delaware's business climate and world-renowned business laws.

Photo: Kevin Fleming.

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ABOUT THIS GUIDE

Delaware Laws & Programs Affecting Business presents an introduction to Delaware and an overview of the laws and programs relating to doing business in the State. Our economy is diverse, and our legal framework is intentionally crafted to foster robust business activity. Our widely copied business laws lead the nation in clarity and predictability.

Government in Delaware is committed to the active promotion of business and economic development in the State. The public and private sectors cooperate in this objective. Governmental incentive programs encourage business to build on and expand Delaware's substantial existing industrial and commercial base.

The information in this guide is presented generally and does not constitute legal, tax, or financial advice on any matter. We have not undertaken to review federal laws or the federal regulatory environment, which are applicable equally in the various states. We do, however, address in this guide the Delaware laws and programs of interest to the conduct of business. Specific inquiries should always be referred to appropriate professionals.

ABOUT RICHARDS, LAYTON & FINGER

Richards, Layton & Finger, Delaware's largest law firm, was founded in the early 1900s and offers a full-service local and regional practice and a national and international practice in the areas of corporate law, corporate litigation, alternative entity law, holding company taxation, and complex financial transactions. With more than 60 percent of the *Fortune* magazine list of the 500 largest corporations in the United States and about one-half of the corporations listed on the New York Stock Exchange being incorporated in Delaware, the firm's corporate clients tend to be national rather than local. The firm represents corporations, limited partnerships, limited liability companies, statutory trusts, and other types of entities in connection with entity governance, mergers and acquisitions, litigation, securities matters, and complex financing transactions on an ongoing basis. Richards Layton is active in bankruptcy, product liability, intellectual property, environmental, media, real property, employment, administrative, and numerous other areas of the law. The firm's tax lawyers handle tax litigation, sophisticated estate planning for individuals, and federal and state tax planning for businesses and individuals.

Richards Layton lawyers are leaders in the profession and in the community. Members of our firm have held the presidency of the Delaware State Bar Association, as well as numerous offices of the American Bar Association, the International Bar Association, and other law-related organizations. Members of the firm have become appellate judges in the state and federal systems. Standard reference works on Delaware law have been authored by the firm's lawyers, including a three-volume treatise entitled *The Delaware Law of Corporations and Business Organizations* and separate treatises on limited partnerships entitled *Delaware Limited Partnerships* and on stockholders' meetings entitled *Meetings of Stockholders*.

The firm is a member of several associations of independent law firms, giving it a global reach. The firm is a member of Lex Mundi, an association of 160 independent law firms with members in more than 100 countries and virtually all U.S. states and Canadian provinces. Richards Layton is also a member of the State Capital Global Law Firm Group, with members located principally in state capitals. Members of Lex Mundi and the State Capital Global Law Firm Group practice independently and not in a relationship for the joint practice of law.

Listing of areas of practice does not represent official certification as a specialist in those areas.

A faint, grayscale background image of the Delaware State Capitol building, featuring a prominent central clock tower with a spire, surrounded by other architectural details and a reflecting pool in the foreground.

CHAPTER ONE

DELAWARE

AN INTRODUCTION

Delaware actively encourages enterprise and investment through modern laws, innovative tax structures, and active cooperation between the public and private sectors.

Midway between New York City to the north and Washington, D.C., to the south, Delaware is centered in the heart of the East Coast. The State is bordered on the north by Pennsylvania and on the west and south by Maryland; on the east, Delaware is separated from New Jersey by the Delaware Bay and enjoys a scenic Atlantic Ocean coastline. Along with several Virginia and Maryland counties, Delaware forms the Delmarva Peninsula.

Delaware ranks 49th in land area among the 50 states, with only 1,955 square miles, and is the sixth least populated state, with approximately 885,122 residents. The State has three counties: New Castle, Kent, and Sussex. Kent and Sussex Counties in the south are historically agricultural, while New Castle County in the north is industrialized. All of the cities and towns in the State are independent, incorporated municipalities. There are three major cities in the State: Wilmington, the State's largest and its legal and financial center; Dover, the State's capital and site of a major U.S. Air Force base; and Newark, the site of the University of Delaware.

Delaware's location allows rapid access to the major metropolitan areas of the Northeast and Mid-Atlantic United States. Nearly one-third of the population of the United States lives within this eastern megalopolis. Interstate and other major highways and frequent passenger rail service provide easy transportation between Wilmington and New York (1 hour, 40 minutes), Washington, D.C. (1 hour, 15 minutes), Philadelphia (30 minutes), and Baltimore (45 minutes). Boston in the north, Raleigh, North Carolina in the south, and Cleveland, Ohio in the west each lie within a 350-mile radius of central Delaware.

Delaware is well served by air transportation, with a close-by network of public and private airports that can readily accommodate commercial and corporate aircraft. Philadelphia International Airport, a major international passenger airport, is a quick, 30-minute drive from downtown Wilmington, and the Baltimore/Washington International Airport is a less than two-hour drive from most locations in Delaware. New Castle County Airport, just 15 minutes from Wilmington, is the base of several large corporate aviation departments and is equipped with complete facilities for major engine and airframe maintenance and repair.

The Port of Wilmington, located at the confluence of the Delaware and Christina Rivers, 65 miles from the Atlantic Ocean, can handle many diverse types of marine freight. Adept at handling automobiles, containers, steel, and lumber, the port is number one in the United States for importing fresh fruit and fruit

juice concentrate and number one in the world for importing bananas. The port covers more than 308 acres and is readily accessible to the east coast of the United States by Interstate 95. Rail access to the port is convenient to each warehouse terminal. Expansion of the storage capacity for existing and future commercial businesses is planned.

Delaware is also served by the main lines of the Norfolk Southern and CSX Transportation railroads. CSX's main line serves New Castle County with connections to Norfolk Southern and the Port of Wilmington. Norfolk Southern serves Delaware over the Amtrak Northeast Corridor and provides service to the entire Delmarva Peninsula. Most of the major industrial sites in Delaware are adjacent to rail lines or have rail sidings at their plant locations. Rail sidings are easily obtainable in Delaware, as compared to other states in the region, due to the lack of rail congestion. In addition to major carriers, Delaware is also served by a number of short-line railroads.

Delaware has major tourist attractions throughout the State, including unique historic sites, museums, mansions, and miles of ocean beaches and bay shoreline. Rehoboth Beach together with the towns of Lewes, Dewey Beach, Bethany Beach, South Bethany, and Fenwick Island comprise Delaware's beach resorts. Rehoboth Beach is a frequent summer vacation destination for Washington, D.C., residents as well as visitors from Maryland, Virginia, and northern Delaware. Vacationers are drawn for many reasons, including the town's charm, artistic appeal, nightlife, and tax-free shopping.

Delaware has one of the strongest economies in the northeast region. Enjoying typically lower than average unemployment, a fair and equitable tax system, and a well-trained workforce, the State's economic climate has shown dramatic improvements beginning in the 1980s, partially in response to stable fiscal policies, careful debt management, conservative spending programs, and personal income tax reductions.

INVESTMENT CLIMATE

Through public and private partnerships, Delaware actively seeks and encourages business and investment. Delaware has developed modern and flexible business organization laws, adopted modern banking and consumer credit laws, reduced personal income taxes, and established a nationwide reputation for an innovative tax structure. As a result of this pro-business climate, more than half of the publicly traded companies in the United States and more than 60% of the Fortune 500 companies are incorporated in Delaware.

Government Sector. Delaware's state government has three branches: executive, legislative, and judicial. The executive power of the government is held by a governor elected every four years and subject to a maximum of two terms. The legislative power of the government rests in a bicameral General Assembly: a 21-member Senate and a 41-member House of Representatives. The entire House stands for reelection every two years, while senators are elected for four-year terms. The General Assembly is in session from the second Tuesday in January until the last day of June in each year; however, the Governor can call a special session of the legislature at any time. The judicial power of the State is exercised by a Supreme Court of five justices appointed for 12-year terms by the Governor and three principal trial-level courts also composed of appointed, term-limited judges. (The judicial system is described more fully in Chapter Eight, **"Dispute Resolution – State Court System."**)

The concept of a public-private partnership, by which government and the private sector work cooperatively to maximize opportunity and the quality of life available in Delaware, is central to Delaware's business and investment climate. This partnership of business and governmental leaders receives overwhelming bipartisan legislative support for programs that strengthen the State's economy.

New taxes or tax increases can only be enacted with a three-fifths majority vote of both houses of the General Assembly. To ensure fiscal integrity and to plan for the future, Delaware is limited to spending 98% of its annual general fund revenues and must maintain a fully financed budgetary "rainy day fund" of 5% of the State's anticipated annual revenue. This fund can be used only to fund an unanticipated budgetary deficiency or to provide funds necessitated as a result of legislation reducing revenue.

Delaware's government accessibility and responsiveness is due in large part to its small size. Industry executives have easy access to the Governor, local government officials, state legislators, and members of the legislature, and governmental red tape is minimal. Legislative initiatives can be refined, developed, and adopted quickly when new ideas will benefit both commerce and the citizens of Delaware generally.

The State also established a Transportation Trust Fund in 1987 to ensure continued funding for Delaware's infrastructure. Through this and other fiscally conservative efforts, Delaware has become a leader in fiscal management. In the spring of 2010, the State received AAA general obligation bond ratings from all three Wall Street rating agencies. Delaware has maintained a triple A

rating since 2001, one of only eight states to hold such a rating for such a long period of time.

Financial Sector. Due in no small part to Delaware's pro-business legal and regulatory environment, strategic positioning, and landmark legislation, dozens of major financial institutions have made Delaware their home. New financial institutions continue to be granted charters in Delaware, including special purpose banks formed through new organizations or acquisitions.

The passage of the Financial Center Development Act in 1981 created strong economic incentives for the banking industry in Delaware, including a favorable state tax structure and the elimination of usury laws. The State subsequently enacted additional legislation in order to sustain the State's competitive advantage in banking. In 1989, the Bank and Trust Company Insurance Powers Act was signed into law, allowing state-chartered banks and trust companies to underwrite and sell various types of insurance. In 1995, the State issued the Incidental Powers Regulation, designed to keep Delaware competitive by allowing state-chartered banks and trust companies to exercise additional powers incidental to banking. In 2006 Delaware's tax structure was modernized, allowing banks to elect an alternate system based on a three-factor income apportionment for multi-state operations. In addition, a location benefit tax reflecting the value of utilizing Delaware's banking laws and bank system was also implemented at that time.

For nearly three decades, Delaware has been world renowned for its banking, financial services, and insurance industries. Partnering with many innovative and dynamic financial companies around the globe, Delaware established itself as the place for international financial institutions looking to enter U.S. markets. As a result, the financial services industry has become a key component of Delaware's economic strength and growth.

As one of the State's largest private-sector employers, the financial services industry is composed of a large, interconnected community of credit card banks, commercial banks, nonbanking financial entities, investment advisors, insurance companies, trust entities, and service providers. In 2010 this industry had over 40,000 employees.

There are currently more than 70 banks and trust companies located in Delaware. They include full-service commercial banks, credit card banks, non-deposit and limited purpose trust companies, wholesale banks, and federal and state savings banks. Credit cards are also a major industry in Delaware and include Bank of America, JP Morgan Chase, Discover Bank, and Barclays

Bank Delaware. Other major bank employers include Wilmington Trust, M&T, PNC, ING Direct, Citigroup, WSFS, Wells Fargo, and HSBC. During the fiscal year ended June 30, 2010, the bank franchise tax contributed \$54 million to the State's revenue.

Tax Outlook. In addition to its modern, flexible business laws and cooperative spirit between business and government, Delaware offers a number of favorable tax advantages, including:

- No state or local general sales taxes.
- No personal property or inventory taxes.
- Exemption for certain investment and holding companies from corporate income tax.
- The State's tax structure follows the federal definition of corporate net income, allowing companies to take full advantage of federal tax law changes.
- Property tax relief for new construction and improvements of existing property.
- The deferment of import taxes at the Port of Wilmington's foreign trade zone.
- Real property taxes that are among the lowest in the nation.
- Public utility tax rebates of 50% on increased consumption for qualifying industries and reduced rate for manufacturers and agricultural processors.
- Accelerated experience rating for new employers.

Labor Outlook. While its ties to the national economy are unmistakable, throughout the recent business cycle Delaware consistently posted lower unemployment rates than the United States. Delaware's unemployment rate as of February 2011 was 8.5%, 1% lower than the national average of 9.5%.

Delaware's nonagricultural labor force totaled approximately 410,700 employees in December 2010. The State's largest industry sector—federal, state, and local government entities—totaled 62,200 employees in December 2010. Total employment in the education and health-care sector remained the State's largest private industry sector, with 59,000 jobs, and retail trade was the second-largest private industry sector, with 48,400 jobs. Over the 12 months from January 2010 to December 2010, the education and health sector was the fastest-growing sector, gaining 1,700 jobs.

Living costs in Delaware are consistently below those of other metropolitan areas. A June 2010 cost-of-living analysis comparing major cities across the nation shows Delaware’s advantage:

Dover, Delaware	100.3	Philadelphia, Pennsylvania	125.0
Wilmington, Delaware	105.2	Newark, New Jersey	127.6
Minneapolis, Minnesota	110.3	Boston, Massachusetts	131.1
Chicago, Illinois	116.8	Los Angeles, California	133.3
Baltimore, Maryland	119.3	Washington, D.C.	139.7
Seattle, Washington	120.2	San Francisco, California	162.5
New Haven, Connecticut	122.3	New York (Manhattan), New York	209.7

Source: ACCRA Cost of Living Index, 2010.

Recent History. In response to recent economic setbacks, Delaware has made important strides to reinvigorate and modernize its manufacturing base. A buyer for the closed Delaware City refinery and Fisker Automotive’s purchase of a former General Motors assembly plant have given those facilities new life. In late 2009, the University of Delaware purchased the 272-acre shuttered Chrysler assembly plant in Newark. The university plans to develop the site.

In March 2010, the U.S. Department of Education announced that Delaware was one of the first two recipients to be awarded “Race to the Top” federal funding. Race to the Top is a federal education funding program that is funded under the American Recovery and Reinvestment Act to reward states for aggressively reforming their education systems. The State will receive \$100 million in Race to the Top funding to implement comprehensive school reform plans over the next four years.

Delaware’s business-friendly legal system continues to attract new corporations. In recent years, more than 70% of new U.S. initial public offerings (IPOs) have chosen Delaware as their legal domicile. The State has continued to register a record number of business formations in the form of limited liability companies and limited partnerships as well.

GOVERNMENTAL BUSINESS INCENTIVE PROGRAMS

Delaware offers an array of programs designed to develop and foster entrepreneurs and small businesses, principally through the Delaware Economic Development Office (DEDO). These range from tax credits, recruitment as-

sistance, and training programs to facilitate bond financing, loans, and venture capital investment. Delaware considers innovative new programs on a continual basis. All programs are periodically reviewed to ensure that they meet changing business needs and may be revised, updated, or eliminated.

The Delaware Economic Development Office. Established in 1981 with a mission to be responsible for attracting new investors and businesses, promoting and developing tourism, and creating new and improved employment opportunities for all citizens of the State, the Delaware Economic Development Office serves as Delaware's central point of contact for business assistance.

Employment and Training Services. The Delaware Economic Development Office's Workforce Center assists Delaware companies in recruiting and retaining valued employees. DEDO will partner with employers and training institutions to conduct targeted marketing programs for specific industries/skill sets—designed to attract and retain a highly skilled workforce. The Workforce Center can also coordinate and fund employment training activities to help new and existing employers achieve company goals.

Through a database of recognized educational resources and training, DEDO can assist when additional or specific labor needs arise for established businesses. Training contracts may be arranged with Delaware colleges, vocational schools, specialized training centers, and independent organizations to provide business, industrial, and service-related instruction. In addition, state funds are available for some employer-provided training programs. Funding amounts are determined by the type of training needed and the availability of other training resources. Businesses are able to select the trainer and maintain total control of the training program.

Recruitment Assistance. Through counseling new and expanding businesses in effective methods and contacts for local employment, the Delaware Economic Development Office helps to recruit a quality workforce for Delaware businesses.

DEDO's website provides assistance to job-seekers and employers through tip-sheets, job postings, and other recruitment tools. Delaware businesses can link to their employment web pages from the DEDO website and sign up to automatically receive resumes from qualified job seekers looking for employment in Delaware.

Small Business LIFT Program. In April 2009, Delaware announced the Small Business Limited Investment for Financial Traction (LIFT). Any Delaware

small business that employs between 3 and 50 persons and has an existing line of credit with a Delaware bank may qualify for the seven-year loan program. The first two years of the loan require no interest or principal payments, and the remaining five years are principal-only payments. The program is expected to help between 200 and 500 Delaware small businesses access as much as \$50 million a year in loans from participating banks. The program is designed to help Delaware's small businesses improve their cash flow, expand their businesses, and become more financially stable.

Tax-Exempt Bond Financing. The Delaware Economic Development Authority can also provide financial assistance to new or expanding businesses, governmental units, and certain organizations that are exempt from federal income taxation by issuing tax-exempt bonds and then lending the proceeds of such bonds. Bond financing applications are reviewed for their financial feasibility and their potential impact on the State's economy.

Business Development and Other Targeted Tax Credits. Delaware provides a number of business development and other targeted tax credits. For information concerning these programs and incentives, see Chapter Four, "**Taxation – Corporate Income Tax – Credits.**"

INSTITUTIONS OF HIGHER EDUCATION

Delaware offers extensive opportunities for higher education through three state-supported institutions and five privately supported institutions. Prominent among these are the University of Delaware, Delaware State University, and Delaware Technical and Community College.

University of Delaware. The University of Delaware was founded as a private academy in 1742 and has grown to become a major research university. As one of the oldest land-grant institutions, the university offers an impressive collection of educational resources. The distinguished UD faculty includes internationally known scientists, authors, and teachers who are committed to continuing the university's tradition by providing one of the highest-quality undergraduate educations available.

UD enrolled more than 21,000 undergraduate and graduate students from diverse backgrounds and a wide variety of geographic regions for the 2010-2011 academic year. Currently, 60% of Newark campus undergraduates are nonresidents who represent nearly every state and more than 50 foreign countries.

Since 1921, UD has been continuously accredited by the Middle States Association of Colleges and Schools. Professional accreditation is also held in Accounting, Agriculture Engineering/Engineering Technology, Athletic Training, Business Administration, Chemistry, Clinical Psychology, Dietetics, Education, Engineering, Family and Community Services, Medical Technology, Music, Nursing, Physical Therapy, and Public Administration.

Thriving research centers and institutes, which now number more than 50 at the University of Delaware, reflect the diversity and rigor of the university's research interests and its commitment to improving the quality of life in Delaware and beyond. To an extent matched by few peer institutions, UD fulfills the Kellogg Commission's model of an "engaged university"—an institution that makes a comprehensive and sustained contribution to the improvement of the communities it serves. The university's research centers increasingly are becoming important state, national, and international assets. UD's faculty attracts significant research sponsorship for projects and programs of student and public benefit, including support for federally funded national centers of excellence. Among the UD faculty are internationally known authors, scientists, and artists, including a Nobel laureate, Guggenheim and Fulbright fellows, a Pulitzer Prize winner, and members of the National Academy of Engineering, National Academy of Sciences, and American Association for the Advancement of Science.

The main campus of the University of Delaware, situated in the northwest corner of the State in the City of Newark, offers a traditional college atmosphere in a location that provides easy access to major cultural and entertainment centers. The I-95 corridor is minutes away from campus. The shore resorts of Delaware, New Jersey, and Maryland and the recreational areas and ski slopes of the Pocono Mountains are about two hours away.

Delaware State University. Delaware State University has a long and proud history as one of America's Historically Black Colleges and Universities. Founded in 1891 as the State College for Colored Students, DSU is one of the country's first land-grant educational institutions, rooted early on in agriculture and education. Over the last 115 years, it has evolved into a fully accredited, 400-acre, comprehensive university with a main campus and two satellite sites. DSU's current population includes a 76% African-American enrollment and an increasing number of Caucasian, Hispanic, and Asian students.

DSU offers 54 undergraduate degree options, 23 master's degree programs, and 5 doctoral degree programs in areas such as interdisciplinary applied

mathematics/mathematical physics and educational leadership. For the 2010-2011 academic year, the student population consists of 3,819 students coming from 35 states and 28 countries. The faculty consists of 205 members from 20 different academic departments.

Delaware Technical and Community College. Delaware Technical and Community College is a statewide institution of higher learning designed to serve business and industry. With its four campuses located in Delaware's three counties—Wilmington and Stanton Campuses in New Castle County, Terry Campus in Kent County, and Jack F. Owens Campus in Sussex County—Delaware Tech is within easy access of all Delaware residents.

Delaware Tech is an open admission institution fully accredited by the Commission on Higher Education of the Middle States Association of Colleges and Schools. Traditional classes are available at the four campuses, and the college's distance learning technologies include interactive classrooms online and telecourses to reach individuals who are not able to attend classes in person. These technologies enable students to take almost any course online.

For more than 40 years, Delaware Tech has been providing education and training to the Delaware workforce. A broad spectrum of skills and information specialists join the Corporate and Community Programs Division to design and conduct job-specific programs for businesses. State and federal funds enable unemployed and underemployed Delawareans to enter specialized programs to receive job skills training or retraining. As employees reenter the labor market, employers gain employees equipped with current job knowledge and practical work experience.

Delaware Tech serves all members of the Delaware community with lifelong learning opportunities: summer camps for children; associate degree programs leading directly to jobs for high school graduates; connected degree programs with area institutions for students seeking bachelor's degrees; basic education, general education development, and industrial training programs for adults in the workplace; and courses designed to enlighten and enrich the lives of retirees.

Privately Supported Institutions. Aside from the three state-supported institutions of higher education, four privately supported colleges and universities enroll approximately 15,000 students in Delaware.

Founded in 1873, Wesley College is affiliated with the United Methodist Church. Located in Dover, Wesley College enrolls about 3,200 students. Approximately half of its students are traditional students—enrolling directly

from high school—while the rest are adult full-time or nontraditional students. The college provides associate, bachelor's, and master's degrees.

Wilmington University has a student body of over 11,000 students at its main campus in Wilmington and at satellite locations throughout the State. Wilmington University is fully accredited by the Middle States Association of Colleges and Schools and offers undergraduate and graduate degree programs.

Goldey-Beacom College is located in Wilmington and provides bachelor's and master's degrees in business. It is accredited by the Middle States Association of Colleges and Schools and the International Assembly for Collegiate Business Education.

Delaware's only law school is Widener University School of Law. With locations in Wilmington and Harrisburg, Pennsylvania, Widener offers students many opportunities for full-time and part-time legal employment while enrolled. Approximately 1,500 students are enrolled at the law school.

CENTERS OF RESEARCH AND TECHNICAL INNOVATION

Ranking second in the nation for number of patents issued per worker, Delaware's economy has long encouraged scientific development. Many of the State's most prominent businesses, such as Agilent, AstraZeneca, DuPont, and W. L. Gore and Associates, are world renowned for their technical breakthroughs and resulting commercial success. Delaware is positioned first in the nation for industry investment and research and development as well as high-wage service jobs, in large part due to the location of these firms in Delaware and the University of Delaware's top-notch research centers. Ranked sixth overall in the 2010 New Economy Index by the Kauffman Foundation and the Information Technology & Innovation Foundation, Delaware has demonstrated its ability to transform from an industrial economic model to one that creates and retains value-added, high-wage jobs. Delaware has consistently ranked in the top 10 and currently ranks first in the nation for high-wage traded services, foreign direct investment, and industry investment in R&D.

The University of Delaware has been classified by the Carnegie Foundation as a research university with very high research activity—a designation given to fewer than 3% of the nation's degree-granting institutions. The university's research office mission is to advance high-quality research and scholarship by promoting an environment that fosters creativity, collaboration, community,

and commitment to the highest ethical values. Through its seven colleges, institutes, and various centers, including the Center for Composite Materials, Center for Catalytic Science and Technology, and Center for Climatic Research, UD has fostered growth and development in the chemical, computer, energy, food, agricultural, and marine sciences industries. UD's Institute of Energy Conversion, one of the world's largest thin-film solar cell laboratories performing research and process development for industry, has been designated by the U.S. Department of Energy as a national center of excellence in photovoltaic research and education. UD's Center for Composite Materials is one of three partners in an Army Research Laboratory Materials Center of Excellence.

Delaware also supports the Delaware Technology Park, home to more than 57 high-tech companies. This partnership of governmental, academic, and private industry provides a location for start-ups in high-technology fields, specifically biotechnology, information technology, and advanced materials. These science-based companies benefit from facilities already set up for science research, an advanced IT infrastructure, and the close proximity of like-minded companies.

Another partner with government, academia, and industry, the Delaware Biotechnology Institute (DBI) has established Delaware as a center for excellence in biotechnology and life sciences. DBI occupies a 72,000-square-foot facility in Newark and is dedicated to enhancing existing academic and private-sector research, catalyzing unique cross-disciplinary research and education initiatives, and fostering the entrepreneurship that creates high-quality jobs. Over the past five years, DBI has successfully built a nationally recognized capability in plant molecular biology to better understand the basic processes that control plant development on the genetic level. Combined with the highly regarded genomics-based poultry disease research located at DBI, this newly developed capability has direct applications to serve Delaware's agricultural industry.

Delaware's support of the sciences has resulted in many firms conducting research and development activities in the State. One is the Fraunhofer Center for Molecular Biotechnology (CMB), which recently received a \$3.5 million grant from the Bill & Melinda Gates Foundation to support the development of transmission-blocking vaccines against malaria. Established in July 2001 as a partnership between the Fraunhofer Society in Germany and the State of Delaware, CMB conducts research in the area of plant biotechnology, developing cutting-edge technologies to assist the diagnosis, prevention, and treatment of human and animal diseases. CMB will use the

Gates Foundation funding to produce lifesaving vaccines in nongenetically modified plants.

Another example of cutting-edge research and development in Delaware is that of NRG Bluewater Wind, one of the nation's leading developers of offshore wind energy projects. Comprised of environmentalists and business professionals, the Bluewater team builds responsible wind energy projects to create clean, reliable energy. In addition to the Mid-Atlantic Wind Park planned off the coast of Delaware, Bluewater is developing projects in New England, the Great Lakes, and Canada.

CHAPTER TWO

BUSINESS ENTITIES



Delaware's business entity laws lead the nation.

Unlike many nations, the United States does not have a single, national law governing the formation and internal governance of corporations and other business entities. Although there is a substantial overlay of federal laws relating to taxation, disclosure, trading of securities, and other matters, under the federal system of government the internal structure and governance of business entities is left primarily to state law. U.S. courts look to the laws of the state of formation of the entity rather than the laws of the seat of management or principal place of business. Therefore, the selection of the jurisdiction in which to form the entity is effectively a selection of governing law and is usually made independently of the place of the entity's operations.

Knowledgeable U.S. and international advisors have long been attracted to Delaware as the forum of choice for formation of business entities. As of June 2010, more than 850,000 business entities had their legal homes in Delaware. Counted among these are 63% of the Fortune 500 companies and more than 50% of all U.S. publicly traded entities.

This attractiveness as the forum of choice for the formation of business entities is no coincidence. Since enactment of its first modern General Corporation Law in 1897, Delaware has offered a liberal, flexible, and nonrestrictive statutory framework that allows investors, entrepreneurs, and managers to fashion their business organizations in the most efficient configuration. The State's business laws are constantly reviewed and adapted to new business and financial developments.

The guiding principle of Delaware's approach is freedom of contract. Businesses are free to choose among different forms of business organization—corporations, general partnerships, limited partnerships, registered limited liability partnerships, statutory trusts, and limited liability companies—in order to match the form of organization to the needs of the enterprise and the intended relationships among its owners, creditors, and management. Furthermore, within each of these general organizational forms there is a broad range of choice as to allocation of authority and control over financial and governance matters.

The attractiveness of Delaware is not limited to the modernity and flexibility of its business organization laws. Delaware also benefits from the expertise of its judiciary in corporate and business matters, the positive attitude toward business and innovation of Delaware's legislature and administration, the state-of-the-art capabilities of the Delaware Division of Corporations, the existence of a large, established body of precedent, and the general familiarity of Delaware

law to corporate practitioners throughout the U.S. and the world. In March 2010, the U.S. Chamber of Commerce's annual poll of corporate counselors and senior litigators found, as in previous years, that Delaware's legal system is the best in the country.

CORPORATIONS

The General Corporation Law of the State of Delaware provides the statutory framework governing the formation of Delaware corporations, the basic relationship between corporations and their stockholders, and the internal governance structure of the corporation.

A corporation may be formed to pursue any lawful act or activity, except as may be otherwise provided by the laws or Constitution of Delaware. A corporation has three primary constituents: stockholders, directors, and officers, plus, under certain circumstances, creditors. In general, stockholders are the owners of the enterprise, directors set the policy for the management of the corporation, and officers run the corporation on a day-to-day basis.

The General Corporation Law also permits the formation of nonstock corporations for profit. These corporations are generally subject to the same statutory scheme as ordinary stock corporations, but with certain significant differences. In 2010, the General Corporation Law was extensively revised to clarify the operation of the law with respect to nonstock corporations. Differences in legal treatment between nonstock corporations and stock corporations are discussed in this chapter under the heading “**Non-stock Corporations.**” Similarly, Delaware permits the formation of close corporations, which are corporations having, among other things, restrictions on the permissible number of stockholders. Close corporations are described in this chapter under “**Close Corporations.**”

STOCK CORPORATIONS

A common form of business organization is the stock corporation. A stock corporation is a corporation organized under the General Corporation Law that has the authority under its certificate of incorporation to issue shares of stock representing the equity interests in the enterprise. The decision whether to form a corporation as a stock corporation authorized to issue shares of stock or as some other type of corporation is entirely up to the organizers of the enterprise and is not a matter dictated by the State or any governmental authority.

Formation. The certificate of incorporation is the basic governing document of the corporation. The information that must be included is narrow in scope: the name of the corporation, the name and address of the corporation's registered agent in Delaware, the purpose for which the corporation is organized (it is sufficient to say that the corporation may engage in any lawful act or activity for which corporations may be incorporated under the General Corporation Law), the number of shares, par value (if any) and terms of the authorized stock, the name and mailing address of the incorporator, and the names and mailing addresses of the persons who are to serve as directors of the corporation if the powers of the incorporator are to terminate upon the filing of the certificate of incorporation. Every certificate of incorporation is deemed to contain the provisions of the General Corporation Law, so it is unnecessary to repeat key provisions of that law in the certificate.

The certificate of incorporation may include any other terms desired so long as these are not contrary to the General Corporation Law. Many of the terms of the General Corporation Law may be varied in the certificate of incorporation, and provisions in a certificate of incorporation may be made dependent on facts ascertainable outside of the certificate of incorporation, such as an agreement among the stockholders of the corporation. Accordingly, broad flexibility is possible. For example, the certificate of incorporation may grant the board of directors the power to adopt or amend bylaws; may increase above a majority the number of votes of directors or shares necessary to take board or stockholder action; may grant or deny preemptive rights; may limit the corporation's term of existence (which is otherwise perpetual); may limit or eliminate the liability of directors for negligent acts; may deny the stockholders the ability to act by written consent; and may make any other provision for the management of the business and for the conduct of the affairs of the corporation that does not conflict with the General Corporation Law.

The corporation is formed, and its existence commences, upon the filing of the certificate of incorporation with the Delaware Secretary of State. It is not necessary to obtain judicial or regulatory approval for the incorporation so long as the certificate of incorporation complies in form with the simple requirements of the General Corporation Law. Often it is possible to form a corporation in a matter of hours. The appointment of an initial board of directors and initial officers, adoption of bylaws, and issuance of shares complete the organization of the corporation.

Limited Liability. The popularity of the corporate form derives principally from two attributes: the separation of ownership from management and the limitation of liability of the stockholders of the corporation. Unless otherwise provided in the certificate of incorporation, the stockholders of a corporation are not personally liable for payment of the corporation's debts. In other words, absent unusual circumstances justifying disregard of the corporate entity, the stockholder is at risk only to the extent of his investment and no more. This concept is critical to the formation of investment capital.

Capital Structure. Delaware does not impose any minimum capital requirements. A corporation is free to establish the capital structure that best suits its needs. Corporations may issue a single class of stock or multiple classes of stock, as the certificate of incorporation provides. The determination of the number of shares of common stock to authorize is primarily a function of the scope of the distribution contemplated for such stock. For a public corporation, there should be authorized sufficient stock to meet the needs of the initial offering as well as sufficient additional shares for future needs, such as acquisitions, employee stock option programs, stock bonuses, and the like. Where the corporation is authorized to issue more than one class of stock, the certificate of incorporation may grant to the board of directors broad powers to fix by resolution the powers, preferences, and rights, and the qualifications, limitations, and restrictions thereof, of any class of stock (including common as well as preferred) where not fixed in the certificate of incorporation. This "blank check" power is often included in the certificates of incorporation of public Delaware corporations with respect to preferred stock.

Stock may be voting or nonvoting, and shares of one class may be given a greater or lesser number of votes per share than shares of another class. Stock may be common stock, standing last in line in the event of liquidation, or preferred stock with a preference over common stock as to dividends, liquidation, or both. The dividend rates of preferred stock may fluctuate in accordance with a formula expressed in the certificate of incorporation or they may be fixed, and stock may be entitled to participate in the earnings of the corporation available for dividends generally or only in a specified portion of those earnings. Stock may be made convertible into shares of a different class and may be made redeemable by the corporation.

Powers. Delaware's General Corporation Law confers on corporations the power to borrow money, guarantee debts, including parent company and sibling-company guarantees, issue bonds, and otherwise incur debt. Although un-

usual in practice, the General Corporation Law permits corporations to create voting debt, that is, debt that carries with it the authority to vote along with stockholders, so long as the certificate of incorporation so provides.

Dividends. Dividends on common stock are normally payable when, as, and if declared by the board of directors, unless restricted in the certificate of incorporation. Dividends on preferred stock are also discretionary unless otherwise provided in the certificate of incorporation. Dividends may be paid out of the net assets of the corporation over and above its statutory capital. (Generally, capital is the aggregate par value of issued par value shares or the issue price of issued no-par shares, unless adjusted by resolution of the board of directors.) If no such funds are available, dividends may be paid out of the net profits of the corporation in the year the dividend is declared and/or the preceding fiscal year, provided that the amount of capital of the corporation following the declaration and payment of the dividend is not less than the aggregate amount of the capital represented by the issued and outstanding stock of all classes of stock having a preference on the distribution of assets. Stockholder approval of proposed dividends is not required, but this requirement may be imposed, if desired, by appropriate provision in the certificate of incorporation.

Management. Unless otherwise specified in the certificate of incorporation, the business and affairs of a Delaware corporation are to be managed by or under the direction of a board of directors. Members of a board of directors are charged with an unyielding fiduciary duty to protect the interests of the corporation and to act in the best interests of the corporation's stockholders. In recognition of the managerial prerogatives granted to directors of Delaware corporations under the General Corporation Law, however, Delaware law generally presumes that, in making business decisions, the directors of a corporation are disinterested and act on an informed basis, in good faith, with due care, and in the honest belief that the action taken is in the best interests of the corporation and its stockholders. Thus, the Delaware courts will not second-guess the business judgments of directors so long as these elements of loyalty and care are present.

The vote of a majority of the directors present at a meeting is necessary to constitute board action unless the certificate of incorporation or bylaws require a greater number. Furthermore, there must be at least a quorum of directors present at the meeting. Unless otherwise provided in the corporation's certificate of incorporation or bylaws, a quorum consists of a majority of the entire board of directors. Directors may also act by written consent

unless prohibited by the certificate of incorporation or the bylaws, but in so acting must be unanimous.

The board of directors may consist of as many or as few natural persons as the certificate of incorporation or bylaws provide. There are no “co-determination” laws, and there is no requirement that any constituency be represented on the board. However, provisions may be made so that the holders of certain series or classes of stock are entitled to elect a specified number of directors, as frequently is the case when investments are made by venture capitalists. In addition, the certificate of incorporation or bylaws may prescribe qualifications for directors, such as requiring that the directors be independent of management or that the directors have a certain level of expertise in the industry in which the corporation operates. The entire board is elected annually, unless the certificate of incorporation provides for the board to be divided into classes. If the certificate of incorporation provides for the board to be divided into classes, directors may be elected for more than one year, with only a portion of the board standing for election each year. The board may not be divided into more than three classes, and directors may not be elected for more than three years. Classification of the board provides for continuity on the board of directors, and directors elected to a classified board can be removed only for cause unless the certificate of incorporation otherwise provides. A classified board prevents stockholders from replacing a majority of the board at a single stockholders’ meeting. Voting in board elections is not cumulative unless the certificate of incorporation so provides.

The corporation’s officers are selected by the board of directors, which also is empowered to remove the officers. Most corporations will have at least a president, treasurer, and secretary, but a corporation is entitled to designate officers with such titles and duties as it may deem appropriate. The authority of the officers is generally fixed in the bylaws or in resolutions adopted by the directors. The officers exercise operational management over the corporation and owe the corporation the same fiduciary duties as directors.

Stockholders. Unless otherwise provided in the certificate of incorporation, stockholders do not manage the corporation. Stockholders elect directors annually and have the power to approve or disapprove significant corporate events, such as amendments to the certificate of incorporation, sales of all or substantially all of the corporation’s assets, mergers, and dissolution. A majority in voting power is required for approval of these matters unless a higher voting requirement is specified in the certificate of incorporation. Directors

are elected by plurality vote, and other matters not specified above may be approved by the vote of a majority of the shares present at a meeting at which a quorum is present, unless the certificate of incorporation or bylaws require a greater vote. With the exception of dissolution by unanimous stockholder approval and short-form mergers of a parent entity holding at least 90% of each class of the subsidiary's voting stock, fundamental corporate changes such as certificate amendments, sales of all or substantially all of the corporation's assets, mergers, and dissolution may not be authorized by a corporation's stockholders without antecedent board action. Stockholders also have the right to adopt, amend, and repeal the corporation's bylaws and to inspect the corporation's and its subsidiaries' books and records for any purpose reasonably related to their interests as stockholders. Stockholders exercise their authority in the form of stockholder resolutions adopted at a meeting, or by written consent (which need not be unanimous), unless the corporation's certificate of incorporation prohibits action by written consent.

Indemnification and Exculpation. Corporations are permitted (and in some cases required) to indemnify directors and officers against liabilities arising out of their official actions. Corporations also may, but are not required to, indemnify employees and agents. Indemnification is not generally permitted for liabilities owed by the directors to the corporation itself, but is available against expenses, judgments, fines, and amounts paid in settlement, in the case of third-party actions, and expenses only, in the case of actions by or in the right of the corporation, which are primarily derivative actions. Corporations may purchase insurance on behalf of directors and officers that may provide coverage for litigation-related losses that extends beyond the indemnification available under the General Corporation Law. In addition, the certificate of incorporation may contain a provision that eliminates or limits the personal liability of a director to the corporation or its stockholders for monetary damages for breach of fiduciary duty as a director, provided that such provision may not eliminate or limit the liability of a director: (i) for any breach of the director's duty of loyalty to the corporation or its stockholders; (ii) for acts or omissions not in good faith or that involve intentional misconduct or a knowing violation of law; (iii) for any liability for declaration of unlawful dividends or unlawful stock repurchases or redemptions; or (iv) for any transaction from which the director derived an improper personal benefit. Many public and private corporations choose to eliminate director liability in its entirety to the fullest extent permitted by law, rather than to limit it to a dollar amount.

Amendments. The certificate of incorporation may be amended as often and in as many respects as the board recommends and the stockholders approve. For example, the certificate of incorporation may be amended to change the corporate name; authorize new classes of stock; reclassify, split, or reverse-split the outstanding stock; alter the management structure of the corporation; or change the powers, preferences, or special rights of any class or series of stock. Amendments are generally effected by the adoption of a resolution setting forth the proposed amendment by the board of directors and declaring its advisability, followed by approval of the amendment by a majority of the outstanding shares entitled to vote thereon. A certificate of amendment must be filed with the Secretary of State thereafter for the amendment to become effective.

Mergers. Of special significance are the provisions of the General Corporation Law relating to mergers. Delaware corporations may merge with other Delaware corporations, with other U.S. corporations, with subsidiary corporations, or with limited partnerships, limited liability companies, or business or statutory trusts; they may even merge with or into non-U.S. corporations. These provisions make possible a broad range of business combinations, allow for change of the corporate structure to a form of entity best suited to meet the parties' business needs, and provide flexibility to move the legal situs of the corporation as may be needed. Mergers are generally effected by the adoption by each of the constituent (merging) corporations of a merger agreement by their boards of directors and approval of the merger by vote of a majority of the outstanding shares entitled to vote thereon. Merger agreements do not require prior approval of judicial authorities, although in certain regulated industries mergers may require governmental approval. A certificate of merger must be filed with the Secretary of State for the merger to become effective. In a merger, the interests of stockholders may be converted into shares of stock of the corporation surviving the merger, into the right to receive cash or other property or securities, or into the right to receive shares of stock of a corporation other than the surviving corporation. Many mergers are structured either as cash-out mergers (in which the target company's shares are converted into cash) or as triangular mergers (in which a target company is merged into a subsidiary of a parent acquiring company, with the target company's shares converting into the right to receive parent company shares).

The General Corporation Law has long permitted a parent corporation owning at least 90% of each class of voting stock of the subsidiary corporation to effect a "short form" merger with the subsidiary merely by action of

the parent company board and filing a certificate of ownership and merger. That authority was recently extended to parent alternative entities, such as limited liability companies.

The General Corporation Law generally provides that dissenting stockholders are entitled to judicial appraisal of the fair value of their shares in cash-out mergers and certain other mergers. A certificate of incorporation also may provide for appraisal rights for any merger or consolidation in which appraisal rights are not otherwise prescribed by the General Corporation Law, or as a result of an amendment of the corporation's certificate of incorporation or sale of all or substantially all of its assets.

Business Combination Statute. Public corporations have the protection afforded by Section 203 of the General Corporation Law unless the company chooses to opt out of Section 203 in its certificate of incorporation. Section 203 generally prohibits a Delaware corporation whose shares are publicly traded from engaging in any business combination with a stockholder who owns 15% or more of a corporation's voting stock for a period of three years following the date that such stockholder became a 15% stockholder, unless one of a number of exceptions applies, such as prior board approval of the business combination. By imposing a three-year moratorium on business combinations with a 15% stockholder, unless a corporation's board of directors approves the business combination prior to the stockholder becoming a 15% stockholder, Section 203 increases the likelihood that a potential acquiror will negotiate with a corporation's management before acquiring a significant block of the corporation's stock. In addition, Section 203 deters two-tiered, highly leveraged takeovers because such acquisitions are frequently financed by junk bonds that are secured by the corporation's assets and intended to be sold upon completion of the transaction to repay the debt.

Sale of Assets. A corporation may sell less than all or substantially all of its assets by action of its authorized officers or its board of directors. A sale of all or substantially all of the assets of a corporation requires the additional approval of a majority of the outstanding shares entitled to vote thereon. There is no bright-line definition of what constitutes substantially all of a corporation's assets, and courts will look to both quantitative and qualitative aspects of the sale (what proportion of assets is being sold and whether the sale fundamentally changes the corporation's business).

Appointment of Trustees or Receivers. The Delaware Court of Chancery has authority to appoint receivers for insolvent corporations. The court

also has authority to appoint custodians for corporations where shareholders are, by reason of deadlock, unable to elect directors, or where directors are unable to take action by reason of deadlock, the shareholders are unable to break that deadlock, and the corporation is facing irreparable harm as a result. The court may also appoint a custodian if the corporation has abandoned its business and has failed to take timely action to dissolve, liquidate, or distribute its assets.

Dissolution. A corporation may be dissolved by adoption of a resolution to dissolve and plan of dissolution by the board of directors and approval of the resolution and plan by a majority of the outstanding shares entitled to vote thereon, or by unanimous stockholder action without prior board action. A certificate of dissolution must be filed with the Secretary of State for the dissolution to become effective.

The General Corporation Law contains two alternate methods of winding up the affairs of dissolved corporations and distributing assets among creditors and stockholders. The simpler of the two alternative methods contemplates that the dissolved corporation will, without judicial involvement, wind up its affairs and distribute its assets to creditors and stockholders in order of the priority of their claims. The second alternative method contemplates public notice, opportunity for filing of claims by creditors or contingent claimants, and judicial involvement in the provision for payment or security for known, contingent, and unknown but anticipated claims. This more complex alternative provides greater protection for stockholders and directors and is often considered in cases of dissolution where extensive present claims exist and future claims may be anticipated, such as in the dissolution of companies that may anticipate significant product liability claims. Both methods are calculated to enable the stockholders and directors of the corporation to limit their post-dissolution exposure to claims of creditors, while at the same time establishing procedures that fairly balance and address the legitimate claims of creditors against the assets of the dissolved corporation.

Taxation. Although a Delaware corporation is subject to federal taxation just as any other U.S. corporation, the extent to which a corporation will be subject to Delaware corporate income tax will depend on the nature and extent of the corporation's activities conducted within Delaware and on whether the corporation qualifies for one of a number of specific categories for which special tax treatment is accorded by Delaware law. At one extreme, a corporation incorporated in Delaware but not doing any business

in Delaware and simply maintaining a statutory corporate office in Delaware is exempt from Delaware corporate income tax. The only Delaware tax on such a corporation is the very modest (as low as \$75 per year) Delaware franchise tax. On the other end of the spectrum, a corporation actively engaged in trade or business activities conducted in Delaware would be fully subject to the Delaware corporate income tax on all of its income.

A corporation that conducts business activities partly in Delaware and partly elsewhere is subject to Delaware corporate income tax on only that portion of its income allocated and apportioned to Delaware under rules specifically set out in the Delaware statutes. Unlike some other states, Delaware does not attempt to apply a unitary or combined reporting tax approach that would subject to Delaware taxation a disproportionate amount of the worldwide income of a corporation that conducts only a part of its business activities within Delaware. Rather, Delaware corporate income tax is calculated strictly under a separate company basis.

Delaware exempts from its corporate income tax corporations commonly referred to as Delaware investment companies (or Delaware holding companies). Delaware investment companies are corporations “whose activities within this State are confined to the maintenance and management of their intangible investments ... and the collection and distribution of the income from such investments or from tangible property physically located outside this State.” For example, a foreign business enterprise desiring to make investments in the U.S. in intangible assets such as stocks, bonds, notes and other debt obligations, patents, trademarks, or copyrights could form a Delaware investment company for the purpose of making such investments without subjecting the income therefrom to state-level corporate income tax.

Delaware investment companies are also expressly exempt from the Delaware gross receipts taxes imposed on various other business taxpayers. Thus, except for the modest annual franchise tax, corporations meeting the statutory definition of a Delaware investment company can, under the right circumstances, be exempt from all Delaware tax. As a result of these rules, a large number of U.S. companies have established Delaware investment companies to which they have transferred investment portfolios, patents, trademarks, or other intangible property for the purpose of eliminating state tax liability on the earnings from those assets. The same opportunity exists for foreign business enterprises that desire to make investments in the United States. (See Chapter Four, “**Taxation – Corporate Income Tax – Delaware Investment Companies.**”)

Domestication and Transfer of Domicile. Of particular interest to non-U.S. corporations, the General Corporation Law permits such a corporation to become a Delaware corporation simply by filing with the Delaware Secretary of State a certificate of domestication and a certificate of incorporation. The certificate of domestication certifies (i) the date and jurisdiction of the establishment of the non-U.S. corporation, (ii) its name immediately prior to such filing, and (iii) the jurisdiction that constituted its principal place of business immediately prior to such filing and set forth in its certificate of incorporation. Upon such filing, the non-U.S. corporation becomes a Delaware corporation, but with its legal existence being deemed to have commenced on the date when the corporation was first formed or established in its original place of organization outside the United States. The Delaware corporation is, in effect, a continuation of the non-U.S. corporation, and all preexisting obligations and liabilities continue unaffected by the domestication. In addition, so long as the laws of the foreign jurisdiction allow it, a foreign entity can be continued as a corporation in Delaware such that both the foreign entity and the Delaware corporation constitute a single entity formed, incorporated, created or otherwise having come into being, and existing under the laws of Delaware and the laws of the foreign jurisdiction simultaneously.

Delaware corporations may domesticate out of Delaware into a non-U.S. jurisdiction. This authority facilitates and simplifies the reincorporation of closely held Delaware corporations into jurisdictions outside the United States. Upon effectiveness of domestication of a Delaware corporation out of Delaware to a non-U.S. jurisdiction, the corporation's existence as a Delaware corporation ceases, but without affecting its existing obligations and liabilities.

Delaware law also provides an explicit mechanism by which a non-U.S. corporation may temporarily transfer domicile to Delaware in the event of an emergency condition in the corporation's home jurisdiction, such as insurrection, war, foreign domination, or expropriation or nationalization of substantial assets.

CLOSE CORPORATIONS

A close corporation is a corporation organized under the General Corporation Law, but whose certificate of incorporation also contains provisions requiring that (i) all of the corporation's shares be represented by certificates and held of record by a specified number of persons, not exceeding 30; (ii) all issued shares be subject to one or more of certain specified restrictions on transfer (such as restrictions granting existing stockholders or the corporation the first

right to purchase shares proposed to be sold by another stockholder); and (iii) there be no public offering of the corporation's shares within the meaning of the Securities Act of 1933, as amended. The certificate of incorporation of a close corporation may set forth the qualifications of stockholders, either by specifying classes of persons who shall be entitled to be holders of record of stock of any class, or by specifying classes of persons who shall not be entitled to be holders of stock of any class, or both. All provisions of the General Corporation Law are applicable to close corporations except as otherwise provided by the General Corporation Law; therefore, the discussion below addresses only the areas of difference. (See “**Stock Corporations**” in this chapter above for generally applicable concepts.)

Formation. A close corporation is formed in the same manner as any stock corporation, except its certificate of incorporation must contain a heading stating that it is a close corporation. The certificate of incorporation must also contain the provisions described above restricting the number of stockholders, the transfer of shares, and the public offering of shares.

An existing corporation that is not a close corporation may convert into a close corporation by amending its certificate of incorporation to contain the foregoing heading and provisions, except that it must be approved by the holders of at least two-thirds of the shares of each class of the stock of the corporation that is outstanding.

Termination of Close Corporation Status. A close corporation maintains its close corporation status until it elects to terminate that status, or until any of the provisions required to obtain that status as set forth in the certificate of incorporation have been breached and neither the corporation nor its stockholders have taken statutorily specified steps to remedy such breach. The Delaware Court of Chancery is given authority to issue orders, upon application of the corporation or a stockholder, to prevent loss of close corporation status by enjoining or setting aside the transaction constituting the breach.

Capital Structure. As noted above, the capital structure of a close corporation is limited on the equity side by the restriction that not more than 30 persons may hold the issued shares. The corporation may refuse to record transfers of stock that would violate the applicable transfer restrictions or result in an excessive number of stockholders.

Management. In an ordinary stock corporation, the management of the business and affairs of the corporation is conducted by or under the direction

of the board of directors, except to the extent specific management functions are expressly conferred on someone else by the certificate of incorporation. In a close corporation, on the other hand, the certificate of incorporation may provide that the stockholders shall manage the business of the corporation directly, in which case no elections of directors are required. Such a provision, if adopted, is required to be noted on every stock certificate to avoid surprise for the unwary. If such a provision is adopted, the stockholders are considered for statutory purposes to be the directors, and the stockholders are subject to the liabilities of directors.

Likewise, the stockholders may, by written agreement among a majority of them, restrict the discretion of directors by providing that the corporation's stockholders or a third party has managerial authority with respect to the operation of the corporation. The effect of such an agreement is to relieve the directors of, and impose upon the stockholders who are parties to the agreement, liability for managerial acts or omissions that would otherwise be imposed on directors to the extent and for so long as the management discretion or powers of the board are controlled by such agreement. No written agreement among stockholders of a close corporation nor any provision of the certificate of incorporation or of the bylaws of the corporation that relates to the affairs of the corporation will be held invalid on the ground that its provisions attempt to treat the corporation as if it were a partnership.

A stockholder may apply to the Court of Chancery for appointment of a custodian or receiver for a close corporation in the event of certain stockholder or director deadlocks, or if such stockholder has been given the option in the certificate of incorporation to compel dissolution of the corporation. In certain similar situations, the Court of Chancery may appoint a provisional director, but such director must be impartial and may not be either a stockholder or a creditor of the corporation.

Dissolution. In contrast to the dissolution provisions governing ordinary stock corporations—which require approval of a resolution to dissolve either by a majority of the board and thereafter by the holders of a majority in voting power of the shares, or alternatively by unanimous stockholder action—a close corporation may include in its certificate of incorporation a provision granting to any stockholder, or to the holders of a specified number or percentage of the shares, an option to dissolve the corporation at will or upon the happening of a specific event or contingency.

NONSTOCK CORPORATIONS

Delaware law permits the formation of nonstock corporations, whether or not organized for profit. In this respect, Delaware law is more flexible than the laws of many other jurisdictions, which may restrict the use of membership corporations to nonprofit or charitable activities. The General Corporation Law distinguishes between nonprofit nonstock corporations, which have memberships, and for-profit nonstock corporations, which have membership interests. While not the prevalent form of business organization, nonstock corporations have been used in a number of for-profit or profit-neutral settings, and some very large and well-known enterprises have been established as nonstock corporations.

Delaware does not have a separate code governing the formation and operation of nonstock corporations, but instead treats these corporations within the framework of the General Corporation Law that also governs ordinary stock corporations. In 2010, the General Corporation Law was extensively revised to clarify further the operation of the General Corporation Law with respect to nonstock corporations. The discussion below addresses the areas of difference in treatment or authority. (See “**Stock Corporations**” in this chapter above for generally applicable concepts.)

Formation. A nonstock corporation is formed in the same manner as a stock corporation, except that in lieu of stating the authorized number, classes, and par value of shares of stock, the certificate of incorporation must state that the corporation has no authority to issue shares of capital stock. The conditions of membership or other criteria for identifying members of the corporation must also be stated in the certificate of incorporation or the bylaws.

Limited Liability. Members in a nonstock corporation are granted the same limitation of liability as stockholders in a stock corporation.

Capital Structure. In view of the absence of authority to issue shares of stock, the statute contains no provisions regarding the capital structure of a nonstock corporation. The concepts of capital and surplus, which find application in stock corporations in the context of permissible sources for payment of dividends and stock redemptions, also apply in the context of nonstock corporations with membership interests except that the capital of a nonstock corporation is deemed to be zero.

Management. The provisions governing boards of directors in stock corporations are generally applicable to nonstock corporations. However, the certifi-

cate of incorporation of a nonstock corporation may provide that the business and affairs of the nonstock corporation shall be managed in a manner other than that applicable to stock corporations. Unless otherwise provided for in the certificate of incorporation or bylaws, nonstock corporations may hold annual meetings of members in accordance with the procedures governing the holding of annual meetings of stockholders of stock corporations, except that all references in the General Corporation Law to stockholders and the board of directors governing such meetings are deemed to refer to the members and the governing body of the nonstock corporation, respectively.

Unless otherwise provided in the certificate of incorporation, (i) the affirmative vote of a majority of the members constitutes the act of the membership; (ii) members of the governing body are elected by a plurality of the votes of the members of the corporation; and (iii) each member is entitled to one vote.

Amendments, Dissolution, and Mergers. In contrast to the procedures necessary to amend the certificate of incorporation of a stock corporation, which require approval of the proposed amendment by the board followed by approval of the holders of a majority in voting power of the voting stock of the corporation, in a nonstock corporation the board has the exclusive power to amend the certificate of incorporation (unless altered by a certificate provision). Likewise, dissolution of the corporation may be authorized by the board alone if there are no members entitled to vote for the election of directors or entitled to vote for dissolution under the certificate of incorporation or the bylaws of the corporation; otherwise, the affirmative vote of a majority of the members having such electoral rights is required. The members may also, by unanimous vote or consent and the filing of a certificate of dissolution, dissolve the corporation without action of the governing body.

A nonstock corporation is authorized to merge with another entity, whether or not a nonstock corporation, and the survivor may be the nonstock corporation or the other entity. To preserve the tax treatment of corporations that are classified as charitable nonstock corporations, mergers between such corporations and for-profit corporations that would destroy the charitable corporation's charitable status are prohibited. Mergers of nonstock corporations must be approved by the affirmative vote of a majority of the members having the right to vote for the election of directors or, if none, a majority of the whole board.

PARTNERSHIPS

A partnership is an association of two or more persons to carry on any lawful business, purpose, or activity. Generally speaking, there are two types of partnerships: the general partnership and the limited partnership. The principal difference between these two forms of partnership is that in a general partnership (subject to certain exceptions) each partner is generally liable for all partnership liabilities, whereas in a limited partnership the limited partners are not so liable.

Delaware has a state-of-the-art limited partnership statute that has been favorably viewed and widely used nationally and internationally because of its flexibility and degree of protection of limited partners from liability for debts of the limited partnership. In keeping with its determination to remain in the forefront of innovation in business laws, Delaware also permits the formation of a limited liability partnership, which is a general partnership in which a partner is not personally liable for the debts of the partnership, and the formation of a limited liability limited partnership, which is a limited partnership in which neither a general partner nor a limited partner is personally liable for the debts of the limited partnership.

GENERAL PARTNERSHIPS

General partnerships are associations of persons who conduct business together, as partners, and who are each subject to joint and several liability for the debts of the partnership. Delaware has adopted a version of the Revised Uniform Partnership Act (DRUPA), which contains rules defining many of the rights and obligations of partners to one another as well as provisions governing the relations of partners to persons dealing with the partnership, property rights of partners, and dissolution and winding up of the partnership.

Formation. A general partnership can be formed orally, by written agreement, or even by the conduct of co-venturers without an express agreement among them to form a formal partnership. To form a partnership it is not necessary to make filings with any governmental agency. However, a general partnership may file a statement of partnership existence with the Secretary of State. If a statement of partnership existence is filed, it must include the name of the general partnership, the address of the general partnership's registered office in Delaware, and the name and address of the general partnership's registered agent for service of process in Delaware. The statement of existence may also include other items.

While DRUPA contains provisions governing the rights and obligations of the partners, these provisions are generally subject to alteration by entry into a written partnership agreement. Although the DRUPA provisions may be adequate for smaller or less complex partnerships, it is usually advisable to enter into a written partnership agreement expressly addressing the relationships of the partners to one another, management of the partnership, the partners' obligations to contribute capital to the partnership, sundry tax matters, the partners' entitlements to shares of partnership profits and losses and distributions from the partnership, the partners' entitlements upon dissolution, and related matters. If entered into, a written partnership agreement does not need to be publicly filed.

Liability. A defining factor of a general partnership is that each partner is generally liable to creditors of the partnership. While in smaller partnerships this may facilitate obtaining credit, it poses a significant risk to the partners. Some insulation from liability may, however, be gained by utilizing a corporation (or other type of entity offering limited liability) as partner such that only the value of the entity's assets is at risk, and not the entire net worth of the individual who is participating in the partnership through the use of the corporation or other entity.

Management. In the absence of an agreement to the contrary, all partners have equal rights in the management and conduct of the partnership business. As to ordinary matters connected with partnership business, a majority vote is sufficient to decide the matter. However, the partners may by their partnership agreement change this management structure and impose any other structure they deem fit.

Partnership agreements frequently alter the management structure established in DRUPA by creating managing partners, altering voting rights to be proportional to contributions or some other economic interest, or otherwise. As with most Delaware business forms, the partners of a partnership are granted broad flexibility in ordering the internal affairs of the entity.

Under DRUPA, unless otherwise provided in the partnership agreement, a partner of a general partnership is entitled to inspect the partnership's books and records for any purpose reasonably related to the partner's interest as a partner in the general partnership. In addition, under DRUPA, partners of a general partnership owe the partnership and the other partners fiduciary duties of loyalty and care. DRUPA permits a partnership agreement to modify these duties; however, a partnership agreement may not eliminate the implied contractual covenant of good faith and fair dealing.

Separate Legal Entity. Under DRUPA, unless otherwise provided in the partnership agreement and a statement of partnership existence filed with the Secretary of State, a general partnership is a separate legal entity. In addition, unless otherwise provided in the partnership agreement and a statement of partnership existence filed with the Secretary of State, a partner of a general partnership is not a co-owner of partnership property and has no interest in specific partnership property.

Capital Structure. Partners are free to establish the capital structure of the partnership. DRUPA does not limit the forms of property that may be contributed to a general partnership. Partners may agree on the contributions that are to be made by each of them, whether or not proportionate to their shares of profits and losses or to their prior contributions. Partners may also agree on their obligations, if any, to make future contributions to the partnership. Partnerships are, of course, permitted to borrow money from partners or third parties or to obtain capital by admitting new partners.

Dissolution. Dissolution of a partnership occurs at the time specified in the partnership agreement or in certain other circumstances. A partnership may also be dissolved by decree of court in certain specified circumstances. Upon dissolution, a partnership is required to wind up its business, liquidate, pay or make reasonable provision for the payment of creditors, and distribute its remaining assets to its partners.

Taxation. Except in the unusual case where a partnership elects to be taxed as a corporation, a partnership is not itself a taxable entity for either federal or Delaware income tax purposes. Rather, each partner's share of profits and losses is passed through to the partner for income tax purposes, whether or not actually distributed to the partner by the partnership. This gives rise to potential tax liability on the part of partners without corresponding cash distributions with which to pay the tax. Partnership agreements typically address and minimize this risk.

A partnership that has filed a statement of partnership existence with the Secretary of State is required to pay a \$250 annual franchise tax to Delaware. (For additional information concerning the tax consequences of partnerships, see “**Limited Partnerships – Taxation**” in this chapter below.)

LIMITED LIABILITY PARTNERSHIPS

Delaware law permits the formation of a form of general partnership known as a limited liability partnership (a DLLP). A DLLP is a type of general partner-

ship in which a partner's general liability is permitted to be restricted. Unless otherwise agreed, a partner of a DLLP, solely by reason of being a partner of the DLLP, is not personally liable for debts of the DLLP incurred while the partnership is a DLLP, whether such debts arise in contract, tort, or otherwise. The DLLP itself, of course, remains liable for its own obligations.

A Delaware partnership may be formed as, or may become, a DLLP. In order to form a DLLP, the original partnership agreement must state that the partnership is formed as a limited liability partnership, and the partnership must file a statement of qualification with the Secretary of State. In order to become a DLLP, the terms and conditions on which the general partnership is becoming a DLLP must be approved by the requisite vote, and the partnership must file a statement of qualification with the Secretary of State. In addition to including the name of the partnership, the address of its registered office in Delaware, and the name and address of its registered agent in Delaware, a statement of qualification must also contain the number of partners of the partnership and a statement that the partnership elects to be a limited liability partnership. In order to remain a DLLP, the partnership must file an annual report with the Secretary of State and pay a fee based on the number of partners of the DLLP. If the DLLP has filed a statement of partnership existence, it must also pay to Delaware an annual \$250 franchise tax.

LIMITED PARTNERSHIPS

Since the Delaware Revised Uniform Limited Partnership Act (the Partnership Act) was enacted in January 1983, Delaware has increasingly become a major forum of choice for the organization of limited partnerships. The Partnership Act has been amended periodically since its enactment to keep it responsive to the needs of entrepreneurs and business leaders.

There are now nearly 93,000 limited partnerships that have been formed in Delaware or have redomiciled to Delaware. The advantages of a Delaware limited partnership include the freedom-of-contract principles that underlie the law of business organizations in Delaware, the ease of forming a limited partnership under the Partnership Act, and the protections contained in the Partnership Act relating to the liability of limited partners.

Formation. A Delaware limited partnership is formed under authority of the Partnership Act. A limited partnership is formed by two or more persons or entities, with at least one general partner and one or more limited partners. The Partnership Act permits a limited partnership to conduct any lawful business, purpose, or activity, with the exception of the business of banking.

It is relatively easy to form a limited partnership under the Partnership Act. Generally, if an understanding exists between at least one general partner and one limited partner concerning the formation of a limited partnership, a limited partnership can be formed by the filing of a certificate of limited partnership with the Secretary of State. As with Delaware corporations, no judicial or regulatory approval is required to create a limited partnership. The required contents of a certificate of limited partnership are likewise few—the name of the limited partnership, the address of the registered office of the limited partnership, the name and address of the registered agent of the limited partnership in Delaware for service of process, and the name and address of each general partner of the limited partnership. Although the original certificate of limited partnership must be signed by all of the general partners, the limited partners need not be listed and need not sign the certificate.

In addition to the certificate of limited partnership, to organize a limited partnership there must be a partnership agreement. While it is generally recommended that a partnership agreement be a written instrument, the Partnership Act does permit oral and implied partnership agreements. Most limited partnerships, however, are governed by a detailed written partnership agreement. For example, a partnership agreement would typically contain provisions addressing the admission of partners, the partners' capital contributions, the rights and powers of partners, indemnification rights, allocation of profits and losses among the partners, distributions to partners, the business to be conducted by the limited partnership, sundry tax matters, and dissolution and winding up of the partnership. In the absence of certain terms of the partnership agreement governing the affairs of the limited partnership, the Partnership Act's default rules will provide such terms. A partnership agreement is not required to be filed with the Secretary of State or any other Delaware governmental agency.

Limited Liability. In a limited partnership, the general partners are generally liable for the debts and obligations of the limited partnership, but the limited partners who do not participate in the control of the business of the partnership have virtually no risk beyond their investment in the limited partnership and are not generally liable for the debts and obligations of the limited partnership.

Management. Typically, the general partners of a limited partnership conduct the day-to-day business and affairs of the limited partnership and are involved in the management of the limited partnership's business. A limited

partner is generally a partner of the limited partnership who does not participate in the management of the business but who invests in the limited partnership in exchange for certain economic rights (including the right to participate in the profits of the business venture).

While a general partner has duties (including fiduciary duties) to a limited partnership and to the other partners, such duties can be modified under the terms of a partnership agreement. Specifically, the partnership agreement may expand, restrict, or eliminate a general partner's duties, but a partnership agreement may not eliminate the implied contractual covenant of good faith and fair dealing. This flexibility is a significant factor favoring the choice of a Delaware limited partnership as a form of business organization.

While a limited partner does not commonly participate in the management of the limited partnership, Delaware law allows limited partners to exercise broad democracy rights without being deemed to be participating in the control (and therefore subject to the liabilities) of the business. For example, limited partners may be independent contractors for or transact business with the limited partnership, an agent, or employee of the limited partnership, or an officer, director, or stockholder of a corporate general partner, without being deemed to participate in the control of the business of the limited partnership. In addition, limited partners of a Delaware limited partnership can consult with and advise general partners on business affairs, can lend money to the limited partnership, can call, request, or attend and participate at meetings of the partners, can serve on committees of the limited partnership, can make determinations relating to investments of the limited partnership, and can take such other actions as may be specified in the limited partnership agreement without being deemed to be participating in the control of the business of the limited partnership. This is a significant advantage of the Delaware limited partnership statute, since limited partners can be actively involved in monitoring their investments in the limited partnership without becoming liable as general partners. In comparison, the limited partnership statutes of many other states significantly restrict a limited partner's ability to participate in management without losing the protection of limited liability.

Reorganization and Dissolution. The Partnership Act permits Delaware limited partnerships to reorganize with or into other types of business entities. Permitting one type of business organization to be converted into another type of business organization as a result of changed circumstances is an important

advantage to using Delaware as the forum for whatever type of business organization is desired. For instance, a Delaware limited partnership may merge with or convert to many other types of business organizations. Many non-U.S. entities can be domesticated into a Delaware limited partnership, and a Delaware limited partnership can be transferred to or domesticated in many jurisdictions outside of the United States.

Dissolution of a limited partnership will occur at the time or upon the happening of an event specified in the partnership agreement or upon the written consent of certain of the partners (depending on the terms of the agreement). Dissolution may occur upon the withdrawal of the last general partner or if at any time there is no limited partner, unless a successor general partner or limited partner, as the case may be, is timely appointed in accordance with the Partnership Act. The limited partnership may also be dissolved on order of a court if it is no longer reasonably practicable to carry on the limited partnership's business.

Taxation. Limited partnerships, like general partnerships, are not ordinarily structured as taxable entities, but rather as conduits or “flow-through entities” for purposes of liability for and payment of income taxes. By comparison, corporate income is potentially subject to double taxation, once at the corporate level (in other words, the corporate entity is itself taxed) and again at the stockholder level when income is distributed to the stockholders in the form of dividends. In contrast, in general under federal tax law, a partnership itself is not subject to income tax, but rather the partners are taxed on their distributive shares of the partnership's taxable income. In addition, cash distributions by a partnership are tax free to the partners to the extent of their respective bases in their partnership interests, and excess distributions are normally taxed at capital-gains rates. In addition, in a partnership, special allocations of profits and losses may be made for tax purposes that are disproportionate to equity interests, so long as the special allocations have substantial economic effect.

Notwithstanding these normal rules of taxation, it is possible for a partnership, whether general or limited, to elect to be taxed as a corporation for both federal and Delaware income tax purposes. Such an election, although fairly rare, may be desirable in order to achieve a particular tax objective.

A Delaware limited partnership or a foreign limited partnership registered to do business in Delaware is required to pay a \$250 annual franchise tax to the State.

LIMITED LIABILITY LIMITED PARTNERSHIPS

Delaware law permits the formation of a form of limited partnership known as a limited liability limited partnership (a DLLLP). A DLLLP is a type of limited partnership in which a general partner's general liability is permitted to be restricted. In a DLLLP, a general partner is not personally liable for the debts of the limited partnership, and no limited partner would have any liability for the debts of the limited partnership even if it participated in the control of the business of the limited partnership. The DLLLP itself, of course, remains liable for its own liabilities.

In order to form or become a DLLLP, in addition to complying with the requirements applicable to forming a Delaware limited partnership, a statement of qualification must be filed with the Secretary of State. An annual report must also be filed in order to maintain a DLLLP's status, and an annual fee based solely on the number of general partners must be paid. A DLLLP must also pay to Delaware an annual \$250 franchise tax.

LIMITED LIABILITY COMPANIES

The Delaware Limited Liability Company Act provides for the formation of limited liability companies, or LLCs, that, if so desired and properly structured, will qualify for flow-through income tax treatment. The owners of a Delaware limited liability company, known as members, will not generally be liable for the debts and obligations of the LLC. This contrasts with limited partnerships, in which there is no taxation at the entity level but liability is not limited as to the general partners, and with corporations, which provide for limited liability of all stockholders but are taxed at the entity level (except in the case of S corporations).

The Delaware Limited Liability Company Act's basic approach is to permit members to have the broadest possible discretion in drafting their limited liability company agreement and to furnish statutory answers only in situations in which members have not expressly included provisions in their limited liability company agreement. Thus, for example, members of an LLC are free to contract among themselves concerning the management of and standards governing the internal affairs of the LLC, including the establishment of classes of members, voting, and procedures for holding meetings of members or considering matters without a meeting. The stated policy of the Delaware Limited Liability Company Act is to give maximum effect to the principle of freedom of contract and to the enforceability of

limited liability company agreements. As a result of this flexible approach, over 530,000 Delaware LLCs have been formed in the 19 years since adoption of the Delaware Limited Liability Company Act.

Formation. A Delaware LLC is a membership entity formed under the authority of the Delaware Limited Liability Company Act. Any natural person, entity, or association may be a member of an LLC. In order to form and organize an LLC, there must be an LLC agreement. While it is generally recommended that an LLC agreement be a written instrument, the Delaware Limited Liability Company Act does permit oral and implied LLC agreements. Most LLCs, however, are governed by a detailed written LLC agreement. The LLC agreement will govern the internal affairs of the LLC and the conduct of its business, but need not be publicly filed.

While an LLC agreement is the cornerstone of an LLC, in order to form a Delaware LLC, one or more authorized persons must also execute and file a certificate of formation. Assuming agreement of the parties to form an LLC, the LLC is deemed to have been formed at the time the certificate of formation is filed with the Secretary of State. However, the LLC agreement can be made effective before, at the time of, or after filing the certificate of formation. A certificate of formation must set forth the name of the LLC, the address of the registered office, and the name and address of the registered agent for service of process on the LLC in Delaware. A certificate of formation may include any other matters that the members determine to include in the certificate.

The Delaware Limited Liability Company Act requires disclosure of only the information needed to put the public on notice of the formation of the LLC. Information such as the identity of the members, their addresses, the amounts of their investments, the nature of the business of the LLC, and the LLC's capital structure need not be set forth in a certificate of formation.

A Delaware LLC may carry on any lawful business, purpose, or activity, with the exception of the business of banking. An LLC agreement should contain provisions dealing with the purposes and powers of the LLC, the powers of the LLC's members and managers, and any desired restrictions on particular LLC activities.

Capital Structure and Management. Members may be admitted upon the later to occur of the formation of the LLC or in the manner provided for in the LLC agreement or, if the agreement is silent, when the person's admission is reflected in the records of the LLC. After the formation of the LLC, a person may be admitted in compliance with the LLC agreement. A person who is not

an assignee of a limited liability company interest will, if the LLC agreement is silent, be admitted to the LLC as a member upon the consent of all of the members and when that person's admission is reflected in the records of the LLC. In the case of an assignee of a limited liability company interest, if the LLC agreement is silent, the assignee will be admitted when its admission is reflected in the records of the LLC. The LLC agreement may provide for different classes or groups of members having differing rights, powers, and duties, including differing voting rights. The LLC agreement may provide for the manner in which profits and losses of the LLC are to be allocated. If the LLC agreement does not contain a provision effectively allocating profits and losses, the statute provides for profits and losses to be allocated on the basis of the value of the contributions made by each member to the LLC as stated in the records of the LLC.

The members of an LLC manage the LLC unless the LLC agreement otherwise provides. The LLC agreement may provide for management by managers rather than by members, and in such case the LLC agreement may specify the responsibilities of the managers and may create classes or groups of managers having differing managerial rights, powers, and duties. The Delaware Limited Liability Company Act provides that to the extent that a member or manager has duties (including fiduciary duties) to an LLC or to another member or manager, (i) any such member or manager acting under an LLC agreement will not be liable to the LLC or to any other members or managers for such member's or manager's good faith reliance on the provisions of the LLC agreement; and (ii) a member's or manager's duties may be expanded, restricted, or eliminated by provisions in an LLC agreement (except an LLC agreement may not eliminate the implied contractual covenant of good faith and fair dealing).

Conversion, Merger, Dissolution, and Term of Existence. The Delaware Limited Liability Company Act contains provisions that authorize an LLC to convert to or from another business entity or to merge or consolidate with or into another limited liability company or other business entity.

The Delaware Limited Liability Company Act provides detailed rules relating to the dissolution and winding up of an LLC. A Delaware LLC has perpetual existence unless otherwise provided in the LLC agreement. Dissolution will also occur on the happening of any event specified in the LLC agreement as a trigger for dissolution; on the written consent of members who own more than two-thirds of the then-current percentage or other interest in the profits of the LLC; at any time there are no members, unless the LLC is continued without

dissolution as provided in the LLC agreement or the Delaware Limited Liability Company Act; or by judicial decree.

Limitation of Liability. As noted, a fundamental policy of the Delaware Limited Liability Company Act is to protect members and managers of LLCs against liability to third parties. The Delaware Limited Liability Company Act provides that, except as otherwise provided in that Act, the debts, obligations, and liabilities of an LLC, whether arising in contract, tort, or otherwise, shall be solely the debts, obligations, and liabilities of the LLC. In addition, the Delaware Limited Liability Company Act provides that, except as otherwise provided by that Act, no member or manager of an LLC shall be obligated personally for any debt, obligation, or liability of an LLC solely by reason of being a member or acting as a manager of the LLC. Thus, regardless of whether a member or manager actively participates in the business of a Delaware LLC or controls a Delaware LLC, such member or manager will not be generally liable for the debts and obligations of the LLC.

Unlike the limited liability company statutes in most states, the Delaware Limited Liability Company Act specifically provides that a member or manager may agree in an LLC agreement or other agreement to be obligated personally for any or all of the debts, obligations, and liabilities of a Delaware LLC. Although it would be rare for an LLC agreement to contain such a provision waiving limited liability, this flexible feature of the Delaware Limited Liability Company Act could be useful in an unusual situation.

Taxation. For federal income tax purposes, an LLC having two or more members will be classified as a partnership unless the LLC elects to be classified as a corporation. An LLC having only one member will be disregarded as a separate entity for federal income tax purposes, unless it elects to be classified as a corporation. The federal tax classification of an LLC also determines its classification for Delaware income tax purposes. A Delaware LLC or a foreign LLC registered to do business in Delaware is required to pay an annual \$250 franchise tax to the State.

STATUTORY TRUSTS

Ordinary common law trusts have been used for centuries to preserve and protect title to property and to minimize taxes. The origins of the modern business trust date back to the early part of the 20th century when they were used as a means of holding real property in jurisdictions where corporations were prohibited. Since that time, the business trust evolved and has been adopted as a

vehicle for investment or the conduct of business and has been used in connection with many diverse business transactions. However, many of the common law rules of trust law are anachronistic and created uncertainty in the context of modern commercial transactions. In 1988, Delaware enacted the Delaware Business Trust Act, which expressly recognized the trust as an alternative form of business entity and created a statutory framework to govern its existence. The principal purpose of the Delaware Business Trust Act was to modernize the common law and provide certainty by codifying Delaware law with respect to the use of trusts in business transactions.

In 2000, the name of the Delaware Business Trust Act was changed to the Delaware Statutory Trust Act, and all Delaware business trusts are now referred to as statutory trusts. The name change was not intended to result in any substantive change in Delaware law; instead, it was intended to eliminate any presumption or inference that a trust formed under the Act is a “business trust” for purposes of Title 11 of the United States Code regarding bankruptcy.

A statutory trust is an unincorporated association that is created by a governing instrument under which property is administered or business or professional activities are carried on by one or more trustees for the benefit of the owners of beneficial interests in the trust property. The Delaware Statutory Trust Act applies to any trust that files a certificate of trust with the Secretary of State.

Delaware statutory trusts are often used as structured finance and asset management vehicles. In the structured finance area, Delaware statutory trusts are used in a wide variety of transaction structures, including leveraged leases, trust preferred security issuances, covered bond transactions, and asset- and mortgaged-backed security issuances. The primary objectives in structured financing transactions are to insulate the property in the statutory trust from a lessee or borrower insolvency and to achieve more favorable tax and accounting treatment than would be the case in a conventional financing transaction.

In the asset management area, in addition to being used to form real estate investment trusts and private investment funds, Delaware statutory trusts are increasingly becoming the entity of choice for the formation of investment companies registered under the Investment Company Act of 1940 and exchange-traded funds. The ability of a Delaware statutory trust to minimize the number of issues that are required to be subject to beneficial owner approval and the absence of any requirement for an annual meeting are significant advantages in terms of cost, particularly given the difficulty with obtaining proxies from retail investors.

Formation. A statutory trust is formed pursuant to a governing instrument and the filing of a certificate of trust with the Secretary of State. The governing instrument may be referred to as a trust agreement, a declaration of trust, or otherwise. There is no requirement that the governing instrument be filed or recorded in Delaware. The certificate of trust must set forth the name of the statutory trust and the name and the business address of at least one trustee who is a resident of or has a principal place of business in Delaware—the latter requirement is not applicable to Delaware statutory trusts registered under the Investment Company Act of 1940. The statutory trust is formed at the time of filing of the certificate of trust.

A statutory trust created pursuant to the Delaware Statutory Trust Act is a legal entity separate and apart from its trustees and beneficial owners. A statutory trust may carry on any lawful business or purpose. The governing instrument of a statutory trust includes the trust instrument itself and may include one or more other documents, such as bylaws.

Except to the extent otherwise provided in the governing instrument of the statutory trust, a Delaware statutory trust has perpetual existence, and the death, incapacity, dissolution, termination, or bankruptcy of a beneficial owner or a trustee will not result in the termination or dissolution of the statutory trust. Upon dissolution at the time set forth in its governing instrument, and after winding up the affairs of the statutory trust, the statutory trust terminates upon the filing of a certificate of cancellation with the Secretary of State.

Except as otherwise provided in the Delaware Statutory Trust Act and the governing instrument, other Delaware laws pertaining to trusts are applicable to Delaware statutory trusts.

Ownership. Beneficial owners are not required to make any contribution to the statutory trust in order to receive a beneficial interest. Beneficial interests in a statutory trust are “securities” for purposes of Article 8 of Delaware’s Uniform Commercial Code. The beneficial interests in a Delaware statutory trust may be evidenced by the issuance of trust certificates or by any other method, such as book-entry registration, in conformity with the applicable provisions of the governing instrument of the statutory trust. Except as otherwise provided in the governing instrument, a beneficial owner is entitled to an undivided beneficial interest in the property of the statutory trust and may share in the profits and losses of the statutory trust in the manner set forth in its governing instrument. A beneficial owner’s interest in a Delaware statutory trust is deemed to be personal property, notwithstanding the nature of the trust property.

The beneficial interests in a Delaware statutory trust may be fashioned to have a broad spectrum of characteristics, free from the traditional constraints of debt and equity interests. Accordingly, new forms of investment securities may be created with separate rights or powers with respect to specified property or obligations of the statutory trust, or profits and losses associated with specified property or obligations, and, to the extent desired, any such investment security may have a separate business purpose or investment objective. A Delaware statutory trust also has many advantages as a bankruptcy-remote vehicle. Because the statutory trust is a legal entity separate from its beneficial owners, the property of the statutory trust is not deemed to be the property of the beneficial owners, and no creditor of a beneficial owner has any right to obtain possession of, or otherwise exercise legal or equitable remedies with respect to, the property of a Delaware statutory trust. Thus, creditors of the statutory trust are more clearly protected from the possibility of a partition of trust property or the premature termination of the statutory trust upon the death, incapacity, dissolution, termination, or bankruptcy of a beneficial owner.

Management. The foremost advantage of the statutory trust is flexibility. The Delaware Statutory Trust Act permits the governing instrument of a statutory trust to establish whatever rights and obligations the trustees, the beneficial owners, and other persons desire. The governing instrument also may provide rights to any other person, including a person who is not a party thereto. This flexibility provides an advantage over alternative forms of business organizations and common law trusts that often are subject to mandatory provisions.

The business and affairs of a Delaware statutory trust are typically managed by its trustees. The governing instrument of a Delaware statutory trust may also include provisions for officers, employees, or other managers of the statutory trust. The governing instrument may also contain provisions defining the rights, duties, and obligations of the trustees, the beneficial owners, and other persons. For example, the governing instrument may provide for classes, groups, or series of trustees or beneficial owners having such relative rights, powers, and duties as are desired by the parties to the governing instrument. The governing instrument of the statutory trust may also provide for the taking of any action, including the amendment of the governing instrument, the accomplishment of a merger, consolidation, or conversion, or the sale or other disposition of all or any part of the trust property, with or without the vote or approval of any particular trustee or beneficial owner, as the parties may desire.

Merger, Consolidation, and Conversion. A Delaware statutory trust may merge or consolidate with, or convert into, any other corporation, limited partnership, limited liability company, or other business entity pursuant to procedures set forth in the Delaware Statutory Trust Act. A merger, consolidation, or conversion may be preauthorized or may be conditioned upon the approval of a specified class or percentage of trustees or beneficial owners or any other person, as set forth in the governing instrument of the statutory trust. If the governing instrument is silent, all of the trustees and beneficial owners must approve the transaction.

Limitation of Liability. Neither the trustees nor the beneficial owners of a statutory trust will have any personal liability for the obligations of the statutory trust unless otherwise provided in the governing instrument. A beneficial owner is entitled to the same limitation of personal liability extended to stockholders of corporations organized for profit under the General Corporation Law. A trustee, when acting in such capacity, will not be personally liable to any person other than the statutory trust or a beneficial owner for any act, omission, or obligation of the statutory trust or any trustee thereof. Moreover, the duties (including fiduciary duties) and liabilities of trustees, officers, employees, managers, or other persons may be expanded, restricted, or eliminated by the governing instrument of the statutory trust (except the governing instrument may not eliminate the implied contractual covenant of good faith and fair dealing).

Taxation. There is no Delaware franchise or other annual tax on statutory trusts formed under the Delaware Statutory Trust Act. In accordance with the desire of the parties, a statutory trust may be taxed for federal and Delaware income tax purposes as a corporation, a partnership, a trust, or otherwise. In addition, a Delaware statutory trust may qualify as a financial asset securitization investment trust (FASIT), a real estate mortgage investment conduit (REMIC), a real estate investment trust (REIT), or a regulated investment company (RIC) under the Internal Revenue Code and thereby receive preferential tax treatment. The ability of a Delaware statutory trust to qualify as a grantor trust for federal income tax purposes has been a driving factor in its use in structured finance transactions for the past two decades.

JOINT VENTURES

A joint venture is a description generally used to denote two or more persons or entities joining together to conduct a specific business. A joint venture may be structured as a corporation, a general or limited partnership, a statutory

trust, or a limited liability company, depending on the degree of integration, management structure, and tax treatment desired. Regardless of the structure of the joint venture, however, certain elements must be present in order for a court to find that a joint venture has been created: (i) equal division of profits and losses, (ii) equal control over the business venture, (iii) equal ownership in the business venture, and (iv) an implicit agreement to engage in the business for mutual benefit.

Delaware entities are often used to structure joint ventures involving international projects or participants. Using a Delaware entity as the joint venture vehicle permits the participants not only great flexibility in structuring the control and economic terms of the venture, but also access to a sophisticated neutral court, the Delaware Court of Chancery, in the event disputes arise over the conduct of the venture or its continuation. In some cases the desire for ready access to an internationally recognized forum that is neither party's home turf has been a deciding influence in choosing to form a joint venture vehicle in Delaware, even if the venture itself does no business in Delaware.

Structural and tax issues should be carefully considered and documented to ensure that the terms of the joint venture are consistent with the expectations of the venturers. Issues such as management of the enterprise, control over use or disposition of contributed assets or technologies, required contributions of capital and permitted distributions of profits, permissibility of alienation of the joint venture interests, and dissolution and winding up of the venture should all be addressed. In some instances, public law will provide some of the requisite mechanisms. For example, Delaware law provides specific mechanisms for dissolving a joint venture organized as a corporation having only two equal stockholders, which might differ from the process that would occur if the joint venture were organized as a partnership, a statutory trust, or an LLC. In addition, depending on the choice of structure, joint venturers may be able to limit or modify their fiduciary duties by contract. In other instances, the venturers will be well advised to handcraft the venture to suit their particular circumstances. Delaware law provides an unparalleled degree of freedom to do this, whichever organizational form is chosen.

NONPROFIT CORPORATIONS AND COOPERATIVES

A Delaware corporation may be structured as a nonprofit entity by including in its certificate of incorporation appropriate language to the ef-

fect that the corporation is not organized for profit and related language limiting distributions of corporate assets to members of the corporation whether on dissolution or otherwise. The General Corporation Law defines a nonprofit corporation as a nonstock corporation that does not have membership interests that are personal property and give members a share of the profits and losses or distributions of a nonstock corporation. Normally, such corporations are conducted for religious, scientific, charitable, or educational purposes.

Although detailed discussion of the tax rules relating to nonprofit corporations is beyond the scope of this guide, it can be noted generally that if certain technical tax rules are followed, a nonprofit corporation can achieve exemptions from both federal and Delaware income tax.

An alternate form of business occasionally used is the cooperative. Except in the case of agricultural cooperatives, which are governed by extensive statutory provisions, the term “cooperative” simply denotes a manner of doing business rather than a distinct organizational form. In this respect, a cooperative is similar to a joint venture. There are no separate Delaware statutes governing, defining, or regulating nonagricultural cooperatives. Such cooperatives tend to be formed as nonstock corporations, a structure that facilitates the timely distribution of any profits as patronage dividends or refunds. Cooperatives are sometimes organized among otherwise independent businesses to effect cost savings or streamline administrative tasks. For example, businesses may form marketing cooperatives, purchasing cooperatives, cooperatives to handle substantially similar administrative processing functions, or other similar cooperatives. Anti-trust considerations must always be kept in mind in considering business cooperatives.

Except in the case of cooperatives for specific purposes organized and operated in conformity with specific federal income tax rules and limitations, the income tax treatment of a cooperative entity depends upon the form of entity employed, be it corporation, partnership, trust, or other type of entity.

SOLE PROPRIETORSHIPS

A sole proprietorship is the simplest form of business enterprise, consisting of a single proprietor conducting business as an individual. A sole proprietorship has no legal existence apart from its owner. No documents are necessary for the formation of a sole proprietorship, although if the business is conducted under a trade or fictitious name, that name will need to be reg-

istered and business licenses may need to be obtained. (See Chapter Three, “**Trade Regulation – Business Name Registration.**”)

Business conducted in this form subjects the owner to unlimited personal liability. Profits and losses of the enterprise are borne directly by the proprietor. Management of the business is entirely within the control of the proprietor, who by definition is the only person with an equity interest in the enterprise. The enterprise itself cannot be sold since there is complete unity between the enterprise and its owner, but the assets used in the enterprise may be sold. A sole proprietorship terminates on the death of the proprietor.

ALTERNATIVE BUSINESS STRATEGIES

Sales Representatives. Businesses located outside of the State of Delaware may choose to send representatives to Delaware to enter into sales contracts for the sale of goods or services. There is no requirement that such a business maintain an office in Delaware. Sales representatives often work from their homes or maintain temporary housing at a central location. Generally, the only requirements imposed on these businesses are those with respect to qualifying or registering to do business in Delaware (see Chapter Three, “**Trade Regulation**”) and those generally applicable to the sale of goods under Article 2 of the Delaware Uniform Commercial Code.

Branch Offices. Many businesses establish branch offices in Delaware to conduct business within the State without forming a separate legal entity in Delaware. This has been accomplished with various types of businesses, including law firms and accounting firms. When a branch office is established, the requirements for qualification or registration to do business in Delaware referenced above must be considered.

Distributors. A manufacturing enterprise may also avail itself of the Delaware market through one or more distributors or franchise distributors. The use of a distributor enables the manufacturer to supply and sell its goods in Delaware without establishing a branch office or hiring sales representatives to travel to or reside in the State. Again, the enterprise must consider whether it will be required to qualify or register to do business in Delaware.

CHAPTER THREE

TRADE REGULATION



Delaware's trade regulation laws balance consumer protection and business interests to maintain a healthy marketplace.

REQUIREMENTS FOR FOREIGN CORPORATION QUALIFICATION

Before a foreign corporation (one organized anywhere other than Delaware) may do business in Delaware, Delaware law requires that it qualify to do business in the State. The qualification is generally required to be made whether the business proposed to be done in the State will be conducted through or by branch offices, agents, or representatives in Delaware.

For a foreign corporation, the process of qualifying to do business in Delaware entails paying a fee and filing with the Delaware Secretary of State a certificate from its jurisdiction of incorporation evidencing its corporate existence and a statement setting forth (i) the name and address of the foreign corporation's registered agent in Delaware, (ii) the assets and liabilities of the foreign corporation as of a date within six months of the filing date, and (iii) the business the foreign corporation proposes to do in the State and a statement that it is authorized to do that particular business in its jurisdiction of incorporation. To maintain its qualification, a foreign corporation is required to file an annual report on or before the 30th day of June in each year. Once the foreign corporation meets the qualification requirements, the Delaware Secretary of State issues a certificate of qualification, which is *prima facie* evidence of the right of the foreign corporation to do business in Delaware. When a foreign corporation registers to do business in Delaware, the corporation consents to the general jurisdiction of Delaware courts.

Delaware law provides for a number of exceptions to the requirement of qualification. Qualification is not required where a foreign corporation merely (i) is in the mail order business accepting orders outside of Delaware and filling them with goods shipped into Delaware; (ii) employs salespersons to solicit orders in Delaware, with all orders approved and all goods shipped from outside Delaware, and with no sales, repairs, or replacements made from stock located in Delaware; (iii) delivers equipment to locations within Delaware pursuant to a contract made outside Delaware, where installation of the equipment requires skilled supervision and such supervision is furnished pursuant to the contract; (iv) is engaged in Delaware in business activities that are wholly interstate in character; (v) is an insurance company; (vi) creates, as borrower or lender, or acquires evidences of debt, mortgages, or liens on property; or (vii) secures or collects debts or enforces any rights in property securing the same.

Foreign corporations that do business in Delaware without having first qualified are subject to fines. A foreign corporation transacting business without having qualified will also be deemed to have appointed the Secretary of State as its agent for service of process in any action against it in Delaware arising out of any business transacted by it in Delaware. In addition, a nonqualified foreign corporation doing business in Delaware is not permitted to bring any action, suit, or proceeding in Delaware until it has been qualified and has paid all fees, penalties, and franchise taxes for the time it did business in Delaware without authority.

REGISTRATION REQUIREMENTS FOR FOREIGN LIMITED PARTNERSHIPS, LIMITED LIABILITY COMPANIES, AND STATUTORY TRUSTS

In order for a foreign limited partnership, limited liability company, or statutory trust (one organized anywhere other than Delaware) to do business in the State, it must comply with the provisions of Delaware law requiring registration with the Secretary of State.

To register, a foreign limited partnership must pay a fee and file with the Secretary of State an application for registration executed by a general partner, setting forth (i) the name of the foreign limited partnership (and any other name it proposes to do business under in Delaware), (ii) the jurisdiction and date of its organization and a statement that it validly exists as a limited partnership under the laws of the jurisdiction where it was organized as of the date of filing, (iii) the nature of the business to be conducted in Delaware, (iv) the address of its registered office and the name and address of its registered agent in Delaware for service of process, (v) a statement that the Secretary of State is appointed the agent of the foreign limited partnership for service of process under certain circumstances, (vi) the name and address of each general partner, and (vii) the date on which the foreign limited partnership commenced or will commence to do business in the State.

A foreign limited liability company desiring to register in Delaware must pay a fee and file an application for registration with the Secretary of State. The application must set forth (i) the name of the foreign limited liability company (and any other name to be used by it to do business in Delaware), (ii) the jurisdiction and date of its formation and a statement that, as of the filing, it validly exists as a limited liability company under the laws of the jurisdiction of its formation, (iii) the nature of the business to be conducted in Delaware, (iv) the

address of its registered office and the name and address of its registered agent in Delaware for service of process, (v) a statement that the Secretary of State is appointed its agent for service of process under certain circumstances, and (vi) the date on which business in Delaware commenced or will commence.

A foreign statutory trust desiring to register in Delaware must pay a fee and file an application for registration with the Secretary of State. The application must set forth (i) the name of the foreign statutory trust (and any other name to be used by it to do business in Delaware), (ii) the jurisdiction and date of its formation and a statement that, as of the filing, it validly exists as a statutory trust under the laws of the jurisdiction of its formation, (iii) the nature of the business to be conducted in Delaware, (iv) the address of its registered office and the name and address of its registered agent in Delaware for service of process, (v) a statement that the Secretary of State is appointed its agent for service of process under certain circumstances, and (vi) the date on which business in Delaware commenced or will commence.

If a foreign limited partnership, limited liability company, or statutory trust doing business in the State of Delaware fails to register as described above, it cannot maintain any action, suit, or proceeding in Delaware until it cures its failure to register and pays all fees and penalties for the time it did business in Delaware without having registered. A fine may be imposed for each year or part of a year during which a failure to register continues.

USURY LAWS

Delaware law provides only limited usury restrictions. There is no limitation on the rate of interest that may legally be charged where (i) the borrower is a corporation, limited partnership, statutory trust, business trust, limited liability company or association, or joint stock company having any of the powers and privileges of corporations not possessed by individuals or partnerships, or (ii) the amount of money loaned or used exceeds \$100,000 and repayment is not secured by a mortgage against the principal residence of the borrower. An individual who has guaranteed the obligations of a corporate borrower may not assert a usury defense, because Delaware law prevents the corporate borrower from doing so.

The State's limited usury restrictions do not apply to loans made by Delaware banks, trust companies, depository institutions organized under federal law and having their principal place of business in Delaware, or lenders licensed under Delaware's Licensed Lender Statute. As a result, Delaware has become

a center for lending by consumer institutions that issue credit cards because these institutions are permitted to export this absence of usury restrictions to credit relationships with customers nationwide.

For the few commercial situations where Delaware’s usury restrictions are applicable, the lender may charge interest at any rate agreed upon in writing not in excess of 5 percent over the Federal Reserve discount rate, including any surcharge thereon. In the event the rate of interest charged exceeds the lawful rate, the borrower is not required to pay the excess and can, at his or her option, retain and deduct the excess from the amount of any debt. If the entire debt is paid with interest exceeding the lawful rate and the borrower brings an action to recover within one year of payment, the borrower may recover the greater of three times the amount of the excess interest or \$500.

BUSINESS LICENSES

In order to engage in most categories of business or occupation in Delaware, a Delaware business license must be procured. The annual fees for these licenses vary depending on the business or occupation and the number of branch offices. In addition, there is normally an additional license fee based on taxable gross receipts or rental payments that varies in rate and amount of allowable exclusions depending on the particular business or occupation. (See Chapter Four, “Taxation – Gross Receipts Taxes.”)

RESTRICTIONS ON SPECIFIC PROFESSIONS

Delaware prescribes standards and restrictions for a wide range of specific professions and occupations. The statutory framework establishes licensing, certification, qualification, and permitting requirements; sets standards for professional schools; and establishes self-governing boards responsible for overseeing the activities of practitioners under their jurisdiction.

Set forth below is a list of some of the more common occupations regulated by Delaware law:

Accountant	Operator of Adult Entertainment Establishment
Architect	Operator of Hotel, Restaurant, or Place of Entertainment
Barber	
Chiropractor	Optometrist
Clinical Social Worker	Pawnbroker
Cosmetologist	Pharmacist

Deadly Weapons Dealer	Physical Therapist
Dentist	Physician
Dietitian	Plumber
Electrical Contractor	Podiatrist
Funeral Service Provider	Private Investigator
Geologist	Professional Counselor
Land Surveyor	Professional Engineer
Landscape Architect	Psychologist
Massage/Bodywork Practitioner	Real Estate Broker
Nurse	Speech Pathologist
Nursing Home Administrator	Veterinarian
Occupational Therapist	

BUSINESS NAME REGISTRATION

Delaware law provides that any person, firm, or association engaging in business in Delaware under a trade or fictitious name must file a certificate with the prothonotary (clerk of the Superior Court) of each county in which such business is being conducted. The purpose of this requirement is to protect consumers from the activities of otherwise unidentifiable persons or organizations engaging in business under other names. The requirement has been held to apply to corporations doing business under fictitious trade names. By analogy, the requirement would also apply to any statutory entity, including a limited partnership, limited liability company, or statutory trust, doing business under a trade or fictitious name that is different from the name recited in its certificate of organization or formation. The registration certificate is a standardized form and includes the disclosure of the trade or fictitious name to be used and the names of the owners of the business. Failure to file may result in a fine.

WARRANTIES

Sellers of goods within Delaware need to be aware of the provisions of Delaware law governing warranties. A warranty is a promise or agreement by the seller that the seller has good title to an article or good or that an article or good has certain qualities. In this context, Delaware law provides for warranties of title, warranties of quality, an implied warranty of fitness for a particular purpose, and implied warranties arising from a course of dealing or usage of trade.

Generally, under Delaware law, a contract for sale includes a warranty by the seller that the seller has good title to the goods being transferred, that the

transfer is rightful, and that the goods are delivered free from any lien or encumbrance of which the buyer has no knowledge. Warranties of title may be excluded or modified only by specific contract language or by circumstances giving the buyer reason to know the seller has no title or that the seller is transferring only such title as the seller has.

A seller may create an express warranty by affirming a fact or making a promise to the buyer relating to the goods that becomes a part of the basis of the transaction between them. In addition, product descriptions and samples or models of the goods that similarly become a part of the basis of the transaction create express warranties that the goods will conform.

Certain warranties about goods may also be implied in a transaction, unless modified or excluded. Where the seller is a merchant of goods of the kind being sold, the seller is deemed to warrant that the goods are merchantable. Delaware law provides standards for determining merchantability and for effectively modifying or excluding an implied warranty of merchantability. Where the seller has reason to know that the buyer will use the goods for a particular purpose and that the buyer is relying on the seller's skill or judgment to select goods suitable for such purpose, the seller is deemed to warrant that such goods will be fit for such purpose. Again, Delaware law provides standards for effectively modifying or excluding the warranty.

The warranties described above extend to the immediate buyer and, in some cases, to third parties. The justification for extending warranties to third parties is that the seller, by marketing its product for use and consumption, has undertaken and assumed a special responsibility toward any member of the consuming public who may be injured by it. Thus, a seller's warranty, whether express or implied, extends to any natural person who may reasonably be expected to use, consume, or be affected by the goods and who is injured by a breach of such warranty.

In an action based on breach of warranty, Delaware law requires the buyer to show not only the existence of the warranty but also that the warranty was breached and an injury or loss was thereby sustained. If these elements are proven, there are certain remedies available to the buyer, including monetary damages or specific performance of the contract.

CONSUMER PROTECTION

Business in Delaware must be conducted with Delaware's consumer protection laws in mind. These laws protect consumers from the intentional false

advertisement of goods. They also prohibit any person engaged in Delaware in the production, manufacture, or distribution of any commodity from intentionally engaging in price discrimination for the purpose of destroying competition. Deceptive trade practices such as passing off goods or services as those of another, deceiving the public with respect to the origin of the goods, or representing that goods are original or new if they are altered, reconditioned, used, or reclaimed are prohibited. Fines may be imposed for violations, and a Delaware court may also award injunctive relief. Similar Delaware law provisions apply with respect to deceptive business practices and unfair trade practices in the insurance industry and the telemarketing industry.

Businesses involved with retail installment sales of goods or services are regulated by laws that impose requirements concerning what is to be included in a retail installment sales contract, insurance, delinquency charges, service charges, refinancings, and monthly statements of account.

REGULATION OF FRANCHISES

Delaware law protects franchise distributors who are economically dependent upon the sale of the franchisor's products and who have used their efforts in promoting the products. A franchise distributor who is unjustly terminated may be entitled to damages or an injunction, which may be issued under principles of equity. Unjust termination includes, among other things, the franchisor's failure to renew the franchise agreement without cause, the franchisor's charging unreasonable or excessive rent for the lease of real or personal property, and the franchisor's failure to renew the lease of such property except upon the payment of unreasonable or excessive rent. Proof of monetary damage, loss of profits, or intent to deceive is not required. A Delaware court may also award reasonable attorneys' fees and expenses for unjustly terminating a franchise.

Some states have passed somewhat more intrusive laws imposing greater restrictions on franchise operations. For example, the laws in some states impose on both parties a duty of good faith in the performance and enforcement of a franchise agreement. Delaware has not yet chosen to enact laws such as these.

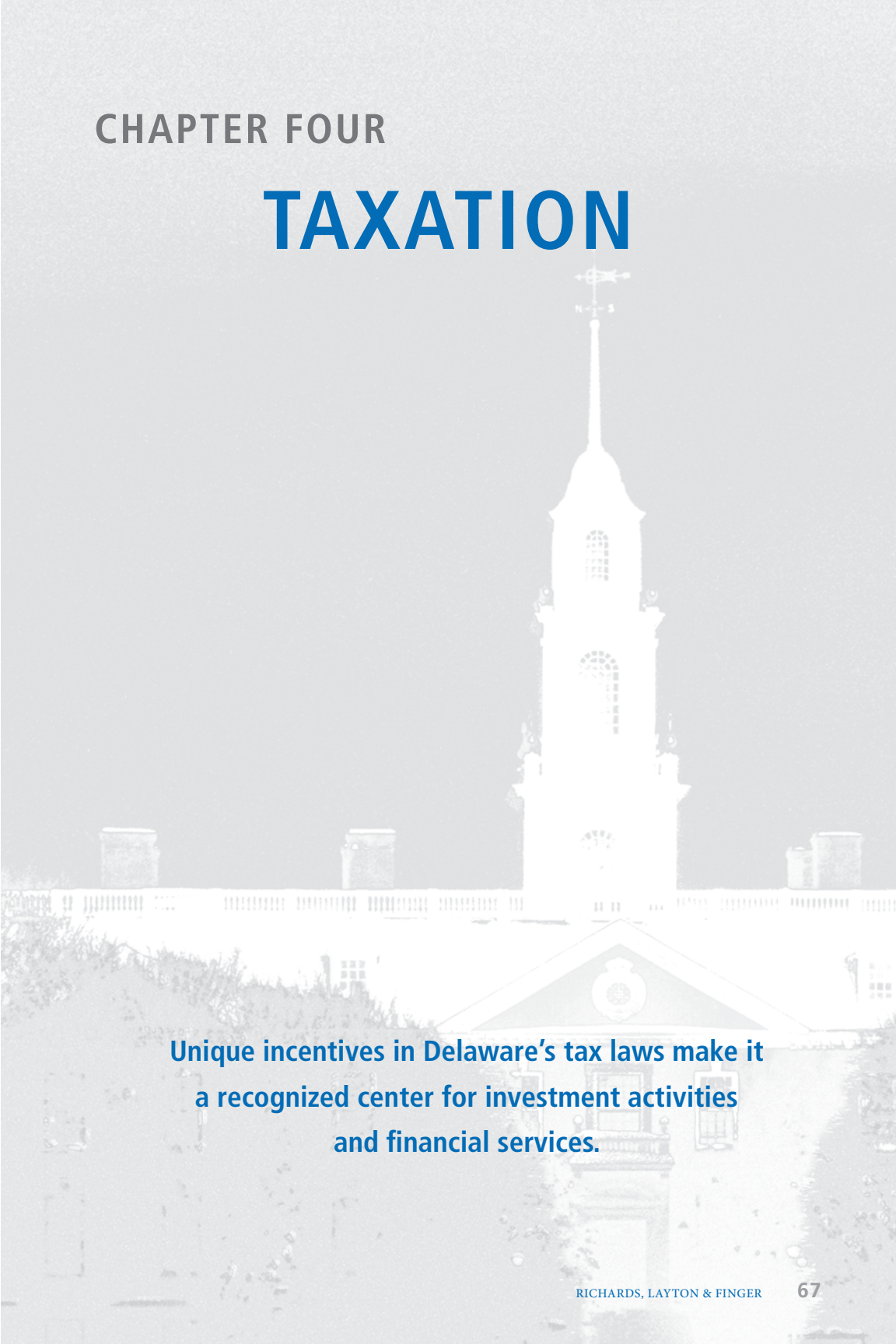
STATE ANTI-TRUST LAW

Delaware's anti-trust statute supplements the substantial anti-trust provisions of federal law. The purpose of the Delaware statute is to promote the public benefits of a competitive economic environment based upon free enterprise. The state anti-trust law protects trade and commerce from unlawful restraints,

price discrimination, price fixing, and monopolies. It is not, however, intended to prohibit the existence of labor organizations and other associations formed for the purpose of mutual help. In addition, the statute does not forbid any conduct or arrangement approved or required by a regulatory board of Delaware or the United States, or a nonprofit corporation, trust, or organization established for religious or charitable purposes (but only to the extent that the activity is religious or charitable in nature). The penalties for a violation of the Delaware anti-trust statute may include monetary civil penalties, equitable relief, or both. Delaware's attorney general may bring suit on behalf of all natural persons residing in the State for a violation of this statute.

CHAPTER FOUR

TAXATION



**Unique incentives in Delaware's tax laws make it
a recognized center for investment activities
and financial services.**

This section contains a general summary of those provisions of Delaware tax law most relevant to investment and business operations in the State. The discussion that follows is necessarily general in nature and is not intended to be an all-inclusive analysis of Delaware tax statutes, rules, and regulations.

PERSONAL INCOME TAX

RESIDENTS

Definition of Residency. Since an individual who is considered to be a state resident is subject to Delaware personal income tax on his worldwide income, while a nonresident is subject to Delaware tax only on Delaware-source income, the determination of whether an individual is a resident of the State is critical. An individual is considered to be a Delaware resident if either (i) he is domiciled in the State, or (ii) he both “maintains a place of abode” in Delaware and spends in the aggregate more than 183 days of the taxable year in the State. An individual is considered to have a Delaware domicile if the State is the place he intends to be his permanent home and to which he intends to return whenever he may be absent. Therefore, an individual who is a permanent resident of another jurisdiction and who is temporarily present in Delaware for business or investment activities will not be classified as a Delaware domiciliary. Further, even if such an individual maintains a place of abode in Delaware, he will not be subject to Delaware personal income tax as a state resident if he is not physically present within the State for more than 183 days during the taxable year. An individual who is present in a foreign country for at least 495 full days in any consecutive 18-month period during which such individual is not present in Delaware for more than 45 days, who does not maintain a permanent place of abode in Delaware at which his spouse, children, or parents are present for more than 45 days, and who is not an employee of the United States government (including service in the armed forces) is not considered a Delaware resident during such 18-month period.

Similarity to Federal Taxation. The computation of the Delaware income tax liability of a state resident is relatively simple and straightforward since Delaware “piggybacks” on the federal income tax system. Delaware taxable income is equal to federal adjusted gross income, with certain modifications discussed below, and less the deductions and personal exemptions allowed by Delaware law.

Delaware Modifications. Delaware law requires a number of additions to and subtractions from federal adjusted gross income in computing Delaware

adjusted gross income. The principal additions include: (i) interest exempt from federal income tax on obligations issued by other states and their political subdivisions, (ii) percentage depletion of oil and gas wells to the extent in excess of cost depletion, and (iii) any net operating loss carryback allowed for federal purposes in excess of \$30,000.

The more significant subtractions from federal adjusted gross income include (i) interest on obligations issued by the United States and its instrumentalities, (ii) refunds of Delaware income tax, (iii) \$2,000 (\$4,000 for a joint return) if certain conditions of age or disability and maximum income are satisfied, (iv) \$2,000 of pension and certain other retirement income (\$12,500 if age 60 or older), (v) social security benefits paid by the United States to the extent included in federal adjusted gross income, and (vi) a carryforward deduction for net operating losses that were precluded from being carried back in previous years because of Delaware's \$30,000 annual limit on net operating loss carrybacks.

Deductions. A Delaware resident may either itemize deductions or claim a standard deduction. The standard deduction is \$3,250, except that in the case of a husband and wife the standard deduction is \$6,500 if a joint return is filed. The standard deduction is increased by \$2,500 for an individual age 65 or over and by \$2,500 for an individual who is blind.

If an election is made to itemize deductions, a Delaware resident's itemized deductions are equal to the sum of his itemized deductions allowable on his federal return, with certain modifications. The principal modifications require reduction of federal itemized deductions by the amount claimed as a deduction for (i) Delaware income taxes, and (ii) income taxes paid to other states and the District of Columbia if a Delaware credit is claimed for such taxes. A husband and wife may elect to itemize deductions only if both do so.

Personal Credits. A Delaware resident is allowed a credit of \$110 for each personal exemption allowable for federal income tax purposes. A Delaware resident age 60 or over is allowed an additional \$110 credit.

Tax Rates. Delaware personal income tax is computed by applying a progressive rate schedule against Delaware taxable income, computed in the manner described above. The lowest rate is 2.2%, and the maximum rate, imposed on Delaware taxable income exceeding \$60,000, is 6.95%.

Credits. A number of credits against the Delaware personal income tax are available. A credit is allowed for taxes paid to states other than Delaware (or

paid to the District of Columbia) on income derived from sources in such other states, subject to limitations. A Delaware credit is also allowed for 50% of the child and dependent care expense credit allowable for federal income tax purposes. A credit equal to 20% of the federal earned income credit is also allowed. In addition, credits against the Delaware personal income tax are provided for (i) donations of land for conservation or historic preservation purposes; (ii) expenditures incurred in the rehabilitation of historic structures; (iii) certain combinations of capital investment and increased employment in the State; (iv) certain reductions of waste release, processing of waste materials, and use of recycled materials certified by the Department of Natural Resources and Environmental Control and by the Delaware Economic Development Office; and (v) qualified investment in certain qualified state businesses certified by the Delaware Economic Development Office. (For certain of these credits against the personal income tax, the rules governing the credits are the same as those for credits against the corporate income tax. See “**Corporate Income Tax – Credits**” in this chapter.)

NONRESIDENTS

An individual not considered a Delaware resident under the definition discussed above is subject to the personal income tax of the State only on his Delaware source income. The method of computing the state tax requires, however, that there be taken into account a nonresident's income from all sources. More specifically, the Delaware income tax of a nonresident individual is computed in the same manner as if he were a state resident (*i.e.*, without regard to source of income), but the amount of tax so computed is then multiplied by a fraction, the numerator of which is the nonresident's modified Delaware source income and the denominator of which is his Delaware adjusted gross income. Delaware adjusted gross income for a nonresident is computed in the same manner as the Delaware adjusted gross income of a resident (*i.e.*, federal adjusted gross income with Delaware modifications). Modified Delaware source income, the numerator of the fraction, is federal adjusted gross income (with the Delaware modifications) only to the extent derived from sources within the State. The effect of this formula is to subject a nonresident's Delaware source income to the same state income tax rate as would be applicable if all of his income were from Delaware sources.

Sources of Income. In computing a nonresident's modified Delaware source income, only those items of income, gain, loss, and deduction entering into his federal adjusted gross income that are derived from Delaware sources (and

that portion of the Delaware modifications that relate to Delaware source income) are taken into account. Items considered to have a Delaware source include those attributable to (i) wages, salaries, and other compensation (other than from pensions) received as an employee for personal services rendered in Delaware (or attributable to employment in Delaware not required to be performed elsewhere); (ii) the ownership or disposition of any interest in real or tangible personal property in the State (including dividends received from a real estate investment trust attributable to rent from, or gain from the disposition of, Delaware real property); (iii) a business, trade, commerce, profession, or vocation carried on in Delaware; and (iv) winnings from pari-mutuel wagering derived from the conduct of pari-mutuel activities within Delaware. A nonresident's modified Delaware source income also includes his distributive share of Delaware source partnership and S corporation income and deductions, and his share of the Delaware source income and deductions of an estate or trust of which he is a beneficiary.

Income from Intangibles. Delaware law provides a favorable rule relating to income from intangible personal property, including interest, dividends, annuities, and gains from the disposition of intangible personal property. Such income is treated as having a Delaware source “only to the extent such income is from property employed by the taxpayer in a business, trade, commerce, profession, or vocation carried on in this State.” Moreover, intangible assets that are treated as held for investment for federal income tax purposes are not treated as so employed by the taxpayer unless they constitute integral parts of the taxpayer's regular trade or business operations. Thus, a nonresident individual's gains from the sale of stock, bonds, or other securities would be subject to Delaware taxation only if such stock, bonds, or other securities were employed by such individual in a Delaware trade or business, which would rarely be the case. As another example, interest income received by a nonresident on a bank or brokerage account maintained in Delaware would not be considered Delaware source income unless the acquisition, management, and disposition of such account constituted an integral part of the taxpayer's regular Delaware trade or business. Further, a nonresident's distributive share of partnership or S corporation income derived from intangible personal property would be considered Delaware source income only to the extent such property was employed by the partnership or S corporation in a Delaware trade or business. These rules make Delaware an attractive jurisdiction for the management of portfolio investments and other intangible personal property.

WITHHOLDING

Every Delaware employer paying wages or other compensation to a resident or to a nonresident who is subject to Delaware income tax is required to withhold tax from such wages or other compensation and pay over the amount withheld to the State.

COUNTY AND MUNICIPAL INCOME TAXES

Counties in Delaware do not have the power to impose any tax upon income. Additionally, except for the State's largest city, Wilmington, no municipality has the power to impose an income tax.

The City of Wilmington imposes an "earned income tax" at the rate of 1.25% on (i) the salaries, wages, commissions, and other compensation of individuals who are city residents, regardless of the place where services are performed; (ii) the salaries, wages, commissions, and other compensation of individuals who are not Wilmington residents for work done or services rendered in the city; and (iii) the net profits of businesses and professions conducted by Wilmington residents or conducted within the city by nonresidents. The Wilmington earned income tax is imposed on individuals, partnerships, associations, and other unincorporated enterprises.

CORPORATE INCOME TAX

Delaware imposes a flat 8.7% corporate income tax on business and investment activity within the State. Federal taxable income, with certain modifications described below, is the base for the Delaware corporate income tax. Since Delaware does not employ a unitary tax system, income allocable to non-Delaware sources is not subject to the Delaware tax. Consolidated and combined returns are neither required nor permitted in Delaware.

MODIFICATIONS

The more significant additions to federal taxable income in computing Delaware taxable income include (i) interest on obligations issued by other states and their political subdivisions, (ii) income taxes paid to any state (including Delaware) or political subdivision, (iii) percentage depletion of oil and gas wells allowable for federal purposes to the extent in excess of cost depletion, (iv) losses from the sale or other disposition of securities issued by the United States or its instrumentalities or by Delaware or its political subdivisions, and (v) any net operating loss carryback allowed for federal purposes in excess of \$30,000.

The more significant subtractions from federal taxable income in computing Delaware taxable income include (i) dividends, interest, and royalties for which foreign tax credit is allowable for federal income tax purposes; (ii) interest income from securities issued by the United States or its instrumentalities; (iii) interest income from advances, loans, and contractual transactions between corporations subject to the Delaware corporate income tax that are eligible to file a consolidated federal income tax return, provided that the paying corporation does not deduct such interest in computing its Delaware taxable income; (iv) gains from the sale or other disposition of securities issued by the United States or its instrumentalities or by Delaware or its political subdivisions; (v) up to \$5,000 of the cost of renovating a building to remove features that restrict use by physically handicapped persons; and (vi) net operating losses that were precluded from being carried back in previous years because of Delaware's \$30,000 annual limit on net operating loss carrybacks.

ALLOCATION RULES

Delaware has not adopted the Uniform Division of Income for Tax Purposes Act, and Delaware law contains specific allocation rules that allocate certain categories of income specifically to Delaware or to another state. Income specifically allocated under these rules is not subject to apportionment under the three-factor formula discussed below. The specific allocation rules allocate (i) rents and royalties (less related expenses) from tangible property to the state in which the property is physically located; (ii) patent and copyright royalties (less related expenses) proportionately to states in which the product or process protected by the patent is manufactured or used, or in which the publication protected by the copyright is produced or printed; (iii) gains and losses from the sale or other disposition of real property (and related expenses) to the state in which such property is physically located; (iv) gains and losses from the sale or other disposition of depreciable tangible property (and related expenses) to the state where the property is physically located or normally used in the taxpayer's business; and (v) interest income (including discount), less related expenses, to the state where the transaction took place that resulted in the creation of the obligation with respect to which the interest was earned. These allocation rules can, in appropriate circumstances, result in income being allocated, for Delaware purposes, to other states even though such income is not subject to tax in such other states.

APPORTIONMENT RULES

If a corporation conducts its entire business operations within Delaware, all of its Delaware taxable income not subject to the specific allocation rules dis-

cussed above is apportioned to Delaware. For those corporations conducting interstate businesses, unallocated corporate income is apportioned to Delaware on the basis of an equally weighted three-factor formula that averages the ratios of (i) Delaware real and tangible personal property to total real and tangible personal property; (ii) Delaware wages, salaries, and other compensation paid to employees within the State to total wages, salaries, and other compensation paid to all employees; and (iii) gross receipts from Delaware sources to total gross receipts. The resulting apportionment percentage is applied to a corporation's entire Delaware taxable income, excluding specifically allocated income. Favorable single-factor apportionment rules are available for asset management corporations, as further described below.

CREDITS

Delaware law provides a number of credits against its corporate income tax, including the following credits of particular interest to businesses:

- **Economic Development Credits.** A \$400 credit for each new qualified employee and an additional \$400 credit for each \$100,000 of qualified investment are available for minimum investments of \$200,000 in a new or expanded facility resulting in the creation of five or more jobs. These tax credits have a 10-year life and are available to (i) manufacturers, (ii) wholesalers, (iii) laboratories or similar facilities for the purpose of scientific, agricultural, or industrial research, development, or testing, (iv) computer processors or data preparation or processing service providers, (v) engineering service providers, (vi) providers of consumer credit reporting services, (vii) wholesale sellers of computer software, (viii) providers of telecommunications services, (ix) providers of aviation services, and (x) administration, management, and support operations (including marketing) for any of the preceding activities.
- **Targeted Area Credits.** The 10-year Economic Development Credits are increased to \$650 for each new qualified employee and \$650 for each \$100,000 of qualified investment if the new or expanded facility is located on or in (i) real property owned by the State or any of its political subdivisions or agencies, (ii) real property owned by non-profit organizations organized and operated solely for the purpose of fostering economic development within Delaware, (iii) any area approved by the U.S. Department of Commerce as a general purpose foreign trade zone, or (iv) any of approximately 30 specified low-income "1990 Delaware census tracts," as defined by the U.S. Department of

Commerce, Bureau of the Census, which are located throughout the State (the Delaware Economic Development Office has maps available of the designated census tracts).

- **Brownfield Credits.** In the case of a new or expanded facility located on a brownfield (defined as a vacant or unoccupied site that the taxpayer reasonably believes may be environmentally contaminated), the \$400 Economic Development Credits are increased to \$650 credits and the \$650 Targeted Area Credits are increased to \$900 credits. For either type of brownfield credit, amounts expended by the taxpayer for environmental investigations and remediations of the brownfield are treated as additional qualified investment.
- **Credits for Commercial or Retail Activities in Low-Income Census Tracts.** A taxpayer engaged in a commercial or retail activity in any of 30 specified low-income census tracts can qualify for the 10-year Economic Development Credits of \$400 for each new qualified employee and \$400 for each \$100,000 of qualified investment.
- **Green Industry Credits.** Manufacturers that reduce chemical wastes by at least 20% or other wastes by at least 50% can qualify for \$400 tax credits for each 10% reduction. These credits have five-year lives. In the case of (i) manufacturers at least 25% of whose raw materials are recycled materials or materials removed from the solid waste stream, (ii) taxpayers engaged in the business of processing materials removed from the solid waste stream for resale as raw materials to manufacturers, and (iii) taxpayers engaged in the business of collecting materials for recycling and distributing recycled materials, Economic Development Credits are available at the increased rate of \$650 for each new qualified employee and \$650 for each \$100,000 of qualified investment (or at the rates of \$900/\$900 if in a targeted area).
- **Research and Development Credits.** A taxpayer may, subject to certain limitations, elect a credit for amounts paid or incurred for research and development equal to (i) 10% of the excess of the taxpayer's total Delaware qualified research and development expenses for the taxable year over its "base amount," as defined for federal income tax purposes but limited to Delaware expenses and Delaware activities, or (ii) 50% of Delaware's apportioned share of the taxpayer's federal research and development tax credit calculated using the alternative incremental credit method. Unused credits may not be carried back but may be carried forward 15 years.

- **New Economy Jobs Program Credits.** Employers who hire at least 50 additional employees (after a base comparison year), each of whom earns annual compensation in excess of \$100,000, are entitled to tax credits equal to a percentage of the Delaware personal income tax withholdings made by the employer with respect to such new employees. In general, an employer is entitled to a tax credit equal to at least 25% of the reasonable Delaware personal income tax withholdings of such new employees for the year of hire and the nine subsequent taxable years. The credit percentage is increased, in some instances up to 65% of such withholdings, in the case of (i) hiring additional employees in excess of 50, and/or (ii) creating those new jobs in either incorporated municipalities, areas designated as brownfields, or targeted growth counties. To the extent the credits exceed applicable Delaware tax liabilities, cash refunds are available. However, no more than 10% of the new employees with respect to which credits are claimed may be persons who were required to file a Delaware personal income tax return in the base year.
- **Business Finder's Fee Credits.** In October 2010, Delaware began a program to incentivize existing Delaware businesses to act as a catalyst for suppliers, customers, and other businesses to relocate to Delaware, resulting in job creation and strengthened supply networks. The Business Finder's Fee Tax Credit provides existing Delaware businesses (sponsor firms) and businesses newly relocating to Delaware (new business firms) eligibility for tax credits of \$500 multiplied by the number of full-time Delaware employees of a new business firm each tax year for three years following the date on which the new business firm is certified in Delaware.

EXEMPTIONS FROM TAX

Delaware law provides complete exemption from state corporate income tax for specific types of corporations or for corporations whose activities within Delaware are limited to certain prescribed activities. Among the more significant exemptions from Delaware corporate income tax are the following:

- A corporation maintaining a statutory corporate office in Delaware but not doing business within the State. As a result of this exemption, a corporation incorporated under the General Corporation Law of the State of Delaware whose only other connections with Delaware are its Delaware registered agent and Delaware registered office is exempt from the state income tax (and all other Delaware taxes other than the corporate franchise tax).

- A Delaware investment company, as further described below.
- A corporation having in effect a valid election under Subchapter S of the United States Internal Revenue Code. Although an S corporation is exempt from Delaware corporate income tax, an S corporation doing business in Delaware that has any nonresident stockholders is required to make estimated personal income tax payments to Delaware on behalf of such nonresident stockholders.
- An entity that is registered as an investment company under the federal Investment Company Act of 1940.
- An entity that qualifies under federal tax law as a real estate investment trust (REIT).
- An entity that qualifies under federal tax law as a real estate mortgage investment conduit (REMIC).
- An insurance company paying Delaware tax on gross premiums, as further described below.
- A banking organization subject to the Delaware bank franchise tax, as further described below.
- A building and loan association subject to the Delaware building and loan association franchise tax.
- A captive insurance company subject to the Delaware tax on premiums, as further described below.

DELAWARE INVESTMENT COMPANIES

The exemption of Delaware investment companies from state corporate income tax (and also from state gross receipts tax) is a feature of Delaware law that has been utilized by thousands of companies (including many Fortune 500 and foreign-based multinational companies) as a means of reducing state income taxes. The statutory definition of Delaware investment companies is:

Corporations whose activities within this State are confined to the maintenance and management of their intangible investments or of the intangible investments of corporations or statutory trusts or business trusts registered as investment companies under the Investment Company Act of 1940, as amended (15 U.S.C. 80a-1 et seq.) and the collection and distribution of the income from such invest-

ments or from tangible property physically located outside this State. For purposes of this paragraph, “intangible investments” shall include, without limitation, investments in stocks, bonds, notes, and other debt obligations (including debt obligations of affiliated corporations), patents, patent applications, trademarks, trade names, and similar types of intangible assets.

A corporation’s qualification as a Delaware investment company is dependent on the nature and extent of the activities engaged in by such corporation within Delaware. So long as a corporation limits its activities within the State to holding and managing its intangible investments and collecting and distributing the income from such intangible investments (or from tangible property physically located outside of the State), complete exemption from Delaware corporate income tax is available.

Delaware investment companies have been used in a wide variety of ways to reduce state income taxes. Among the more common uses of Delaware investment companies are the following:

- The holding of stock, bonds, notes, certificates of deposit, and other portfolio assets. The dividends, interest, and other income received by a Delaware investment company from such assets are exempt from Delaware corporate income tax and can avoid income taxes imposed by other states.
- The holding of patents, trademarks, copyrights, and other intellectual property, and the licensing of the use of such intellectual property in exchange for the payment of royalties or license fees. Not only is there exemption from Delaware income tax for such royalties and license fees, but also the licensee, under appropriate circumstances, may be able to deduct the royalty or license payments in computing its liability for state income tax in those jurisdictions in which the licensee is subject to tax.
- The sale of unwanted intangible assets without Delaware income tax on any gain from such sale and without, in appropriate circumstances, income taxes that might otherwise be imposed upon such gain by other states.
- The making of loans to an affiliate, thereby generating, in appropriate circumstances, an interest-expense deduction to the affiliate in its domiciliary jurisdiction without the interest received by the Delaware investment company being subject to Delaware income tax.

ASSET MANAGEMENT CORPORATIONS

Effective for taxable years beginning after 2008, a corporation that qualifies as an asset management corporation can elect to apportion its Delaware taxable income solely on the basis of the ratio of its Delaware source gross receipts from asset management services to its total gross receipts from asset management services. The single-factor apportionment rules available to asset management corporations make Delaware an attractive jurisdiction for the location of financial service companies.

For a corporation to be eligible to elect asset management corporation classification, it must derive 90% or more of its gross receipts, as reported for federal income tax purposes, from asset management services. Such services are services rendered with respect to intangible investments that, in general, constitute rendering investment advice, determining the timing of purchases and sales, purchasing and selling intangible investments, providing certain specified administration and distribution services, and managing contracts for subadvisory services. Of particular significance is that the source of gross receipts from asset management services is generally based on the domicile of the consumer of such services. Thus, an asset management corporation would, in general, be subject to Delaware corporate income tax only to the extent it provided services to individuals and entities domiciled in Delaware.

HEADQUARTERS MANAGEMENT CORPORATIONS

A headquarters management corporation (HMC), although not exempt from Delaware tax, is subject to a favorable tax regime in Delaware. An HMC, in addition to engaging in the traditional activities of a Delaware investment company of maintenance and management of intangible investments, can also provide services to affiliated entities. An HMC's taxable income is subject to Delaware tax at a rate of 8.7%. However, the resulting Delaware tax liability of an HMC can be reduced in each of its first 10 years of qualification as an HMC by up to an aggregate 99% reduction (i) at the rate of 20% for each full-time employee of the HMC in Delaware, and (ii) at the rate of 2% for each \$7,500 of qualified expenditures in Delaware. In addition, a \$400 credit is allowed in each of the first five years in which an HMC employs five or more qualified employees for each such employee who is a new employee. An HMC is, however, subject to an annual minimum tax of \$5,000 and must also pay to the State a \$5,000 annual license fee. An HMC is exempt from the payment of gross receipts tax.

BANKING ORGANIZATIONS

In lieu of the Delaware corporate income tax, a bank, trust company, other banking organization, and any subsidiary corporation of a banking organization is liable for a Delaware franchise tax on taxable income. For this purpose, taxable income is defined as 56/100th of 1% of net operating income before taxes, with certain modifications. The Delaware bank franchise tax employs a regressive rate schedule with a maximum rate of 8.7% of taxable income not in excess of \$20 million and a minimum rate of 1.7% of taxable income in excess of \$650 million. Since the tax may be computed on a basis that consolidates the income of a banking organization with the income of its subsidiary corporations, the tax advantage of this regressive rate schedule can be maximized.

In lieu of the bank franchise tax computed on taxable income as described above, a banking organization or trust company can elect an alternative bank franchise tax calculation that is the sum of (i) an income tax employing a three-factor apportionment, but with the gross receipts factor double weighted, computed by applying regressive rates ranging from 7% (of taxable income not in excess of \$50 million) to 0.5% (of taxable income in excess of \$1.3 billion); and (ii) a “location benefits tax” based on net assets, with a minimum tax of \$2 million and a maximum of \$8.25 million.

A credit of \$400 is available for each new bank employee in excess of 50 for which the banking organization has invested at least \$15,000. This new employment credit is available whether the bank franchise tax is computed in the traditional manner based on taxable income or by using the alternative method.

INSURANCE COMPANIES

In lieu of the Delaware corporate income tax, an insurer doing business in Delaware, other than a captive insurance company, a workers’ compensation insurer, or a wet marine and transportation insurer, is liable for a general premium tax of 2% (1.75% pursuant to 18 Del. C. § 702 + 0.25% pursuant to 18 Del. C. § 707) on net premiums from policies covering Delaware risks. Most insurers chartered under Delaware law (other than certain mutual insurers) having annual gross receipts of \$1 million or more are also required to pay annual Delaware “privilege taxes” ranging from a minimum of \$10,000 to a maximum of \$95,000.

CAPTIVE INSURANCE COMPANIES

In lieu of the Delaware corporate income tax, a captive insurance company is liable for tax at the rate of 2/10th of 1% of the direct premiums collected dur-

ing each calendar year on policies and contracts written by the company (less return premiums paid to policyholders), up to a maximum tax of \$125,000. A tax at the rate of 1/10th of 1% is imposed on the assumed reinsurance premiums collected by a captive insurance company during each calendar year, up to a maximum tax of \$75,000. The annual minimum aggregate tax payable by a captive insurance company is \$5,000, and the annual maximum aggregate tax is \$200,000 (only \$50,000 in the case of a captive insurance company with at least 25 full-time employees in Delaware).

CORPORATE FRANCHISE TAX

A corporation incorporated in Delaware, if not exempt, is required to pay an annual franchise tax to the Delaware Secretary of State on or before the first day of March.

EXEMPT CORPORATIONS

Delaware law provides that a number of classes of corporations are exempt from the franchise tax. The more significant exemptions are for banking corporations, savings banks, building and loan associations, and religious, charitable, and nonprofit corporations.

METHODS OF COMPUTING TAX AND RATES

The Delaware corporate franchise tax is computed under two alternative methods. A Delaware corporation may elect the method that produces the lesser amount of tax.

Authorized Shares Method. Under this method, the franchise tax is determined solely by reference to the number of shares of capital stock authorized in a Delaware corporation's certificate of incorporation. The minimum annual tax under this method is \$75 where authorized capital does not exceed 5,000 shares; for authorized shares above 5,000 shares, the tax is \$150 plus \$75 for each 10,000 shares, or part thereof, in excess of 10,000 authorized shares.

Assumed Par Value Capital Method. Under this method, the tax is determined under a formula by reference to a Delaware corporation's number of authorized shares of capital stock without par value, number of authorized shares of capital stock with par value, and total gross assets.

Minimum and Maximum Tax. Regardless of which of the two methods is used, in no case will the franchise tax for a full taxable year be more than \$180,000 or less than \$75. The minimum \$75 tax can be assured by limiting the number of shares of capital stock, whether with or without par value, autho-

rized in a Delaware corporation's certificate of incorporation to 5,000. Where a corporation has not been in existence during an entire year, the amount of tax otherwise due, as computed in the manner described above, is prorated for the portion of the year during which the corporation was in existence.

Regulated Investment Companies. The franchise tax paid by a Delaware corporation that is a regulated investment company for federal income tax purposes is the least amount of tax computed under the authorized shares method, the assumed par value capital method, or \$350 for each \$1 million, or part thereof, of its average gross assets (the mean of gross assets on January 1 and December 31). The maximum franchise tax payable by a regulated investment company is \$90,000.

GROSS RECEIPTS TAXES

In order to conduct business within Delaware, most occupations and businesses are required to obtain a license from the State. (See Chapter Three, “**Trade Regulation – Business Licenses.**”) Although annual license fees are minimal, most types of businesses are also required to pay a gross receipts tax. This subsection addresses the gross receipts taxes applicable to those types of commercial enterprises that are of the most general interest. Readers are cautioned that various specific categories of businesses are subject to state gross receipts taxes that are not discussed below.

GENERAL OCCUPATIONAL AND SERVICES TAX

A tax equal to 0.4147% is imposed by Delaware on the aggregate monthly gross receipts, less an \$80,000 monthly deduction, of every person engaged in one of a lengthy list of enumerated occupations and on every other person engaging “in any service industry, business, calling or profession” not included within one of the enumerated occupations. Gross receipts for purposes of this tax is defined generally as “total consideration for services rendered, goods sold, or other income-producing transaction within this State, including fees and commissions.” A number of occupations and businesses are specifically exempt from payment of the general occupational and services gross receipts tax, including, most notably, Delaware investment companies, headquarters management corporations, banks, insurance companies, public utilities, savings and loan and building and loan associations, nonprofit organizations exempt from federal income tax, real estate mortgage investment conduits, and Delaware statutory trusts registered as investment companies under the Investment Company Act of 1940.

MANUFACTURERS' TAX

A person engaged in manufacturing in Delaware is liable for a state tax equal to 0.1944% of aggregate monthly gross receipts, less a monthly deduction of \$1 million. For purposes of this tax, gross receipts includes, in general, all proceeds received for products manufactured in whole or in part within the State if such products are sold to another person, or the fair market value of any such products consumed by the manufacturer or an affiliate. If a product is manufactured only partially in Delaware, gross receipts from the sale of the product are apportioned on the basis of the ratio of manufacturing costs within Delaware to total manufacturing costs.

RETAIL AND WHOLESALE MERCHANTS' TAXES

Wholesalers. A wholesaler is, in general, a person selling or exchanging goods for the purpose of resale by the person acquiring such goods. A wholesaler is liable for Delaware tax in an amount equal to 0.4147% of aggregate monthly gross receipts, less an \$80,000 monthly deduction. For purposes of the wholesalers' tax, gross receipts is defined to include total consideration received from sales of tangible personal property physically delivered within Delaware. Special rates are applicable to food processors (0.2074%) and commercial feed dealers (0.1037%), both with the standard \$80,000 monthly threshold.

Retailers. A retailer is defined, in general terms, as a person selling or exchanging goods "on the assumption that the purchaser of such goods has acquired the same for ultimate consumption or use and not resale." A retailer is subject to a tax of 0.7776% of aggregate monthly gross receipts, less an \$80,000 monthly deduction. For purposes of the retailers' tax, gross receipts is defined to include total consideration received for all goods sold or services rendered within the State. Special rates are applicable to restaurant retailers (0.6739%), grocery supermarkets (0.3402% on first \$2 million per month and 0.6372% thereafter), and farm machinery retailers (0.1037%), all with the standard \$80,000 monthly threshold.

GROSS RECEIPTS TAX REDUCTIONS

Taxpayers qualifying for Economic Development Credits (see "**Corporate Income Tax – Credits**" in this chapter above) also qualify for reductions in the general occupational and services, manufacturers', and retail and wholesale merchants' gross receipts taxes during the 10-year life of the Economic Development Credits. Such categories of gross receipts taxes are reduced by 90% for the year in which the new or expanded facility is placed in service, and the reduction decreases (generally by 10%) in each of the succeeding nine years. In

the case of taxpayers qualifying for Targeted Area Credits, such gross receipts taxes are eliminated completely for the first five years and are subject to percentage reductions in each of the next nine years.

CONTRACTORS' TAX

A contractor is defined as any person engaged in furnishing labor or both labor and materials in connection with any construction, alteration, repair, or demolition of any type of structure. The definition includes both contractors and subcontractors, but a contractor can exclude from gross receipts amounts paid to a subcontractor who is himself subject to the contractors' tax if there is a written agreement between the contractor and the subcontractor setting forth the exact sums payable to the subcontractor. A contractor is liable for Delaware tax equal to 0.6739% of aggregate monthly gross receipts, less a monthly deduction of \$80,000. For purposes of the contractors' tax, gross receipts generally includes all sums received for any work done or materials supplied in connection with any real property located in Delaware.

AFFILIATED FINANCE COMPANY TAX

For purposes of Delaware's system of gross receipts taxation, a corporation classified as an "affiliated finance company" constitutes a special class of taxpayer that is exempt from the normal gross receipts taxes but is subject to a flat annual fee, ranging from \$10,000 to \$50,000, based on the corporation's "capital, surplus and retained earnings, or equivalent accounting terms, as set forth in the company's certified financial statements." An affiliated finance company is defined as a corporation substantially all of whose activity within Delaware is limited to the issuance of commercial paper or other debt obligations and the use of the proceeds to make loans to, or to purchase receivables from, one or more of its affiliated corporations (defined as two or more corporations that are members of a controlled group of corporations for federal income tax purposes). The exemption from normal gross receipts taxes for affiliated finance companies makes Delaware an attractive jurisdiction for a parent corporation seeking to establish a financing subsidiary. This is particularly true in light of the Delaware corporate income tax exclusion of interest income received from an affiliated corporation that does not deduct such interest in computing its Delaware taxable income.

PROPERTY TAXES

No state tax is imposed on any real or personal property in Delaware. In addition, no county or municipality is authorized to assess ad valorem taxes on personal property.

Real estate is subject to county property taxes, school district property taxes, vocational school district taxes, and, if located within an incorporated area, municipal property taxes. The total property tax burden depends on the tax rate, the property assessment, and the assessment ratio, and these factors vary from location to location within Delaware. In general, the effective tax rate ranges from 0.4% to 1.2% of market value. Delaware real property taxes are significantly below the national average and those imposed in surrounding states. Indeed, real estate taxes in Delaware are among the lowest of any state.

Delaware employs the same real estate tax structure for both commercial and residential property. Therefore, Delaware businesses can take advantage of the same low property tax rates that homeowners enjoy. No tax is imposed on inventories by the State or any county or municipality.

SALES AND USE TAXES

Delaware does not impose a general sales or use tax. Further, counties and municipalities within the State are not authorized to assess a general sales or use tax. Consequently, retailers in Delaware enjoy a significant tax advantage over retailers in surrounding states.

TAXES ON SPECIFIC PRODUCTS AND SERVICES

A very limited number of specific products and services are subject to special Delaware taxes, including taxes on the sale or use of cigarettes (8 cents per cigarette, being \$1.60 per 20-cigarette pack) and other tobacco products (15% of wholesale price), gasoline (23 cents per gallon, with exemptions for certain sales), alcoholic beverages (different rates on beer and wine and various rates on other spirits depending upon alcohol content), public accommodations (8% of the room charge), and motor vehicles (3.75% of purchase price).

USE TAXES ON LEASES OF TANGIBLE PERSONAL PROPERTY

The State imposes a use tax on lessees of tangible personal property. Leases of a number of categories of property are excepted, including household furniture, fixtures, and furnishings, and hospital and medical equipment. If this use tax is applicable, it is imposed at the rate of 2.0736% of the rent under a lease for the use within Delaware of tangible personal property. In addition, lessors of tangible personal property are subject to a lessor's tax at the rate of 0.3110% of lease rental payments received in excess of \$240,000 per quarter.

REALTY TRANSFER TAX

The State imposes a tax of 2% of value upon the transfer of real estate. Unless otherwise agreed by the parties, the realty transfer tax is shared equally by the grantor and grantee. The Delaware statute provides a lengthy list of specific real estate transactions that are exempt from the state transfer tax.

State law authorizes municipalities to impose realty transfer taxes of up to 1.5%, and most municipalities have done so. Similarly, counties are authorized to impose realty transfer taxes of up to 1.5% with respect to property in their unincorporated areas. All three counties in the State have imposed 1.5% taxes. Where a transfer of real estate is subject to either a municipal or a county transfer tax of the full 1.5% allowable, the realty transfer tax payable to the State is reduced from 2% to 1.5%, making the aggregate transfer tax that is payable 3% of value.

A faint, grayscale background image of the Delaware State Capitol building, featuring a prominent central clock tower and a pedimented entrance.

CHAPTER FIVE

LABOR AND EMPLOYMENT

Delaware's employment laws avoid burdensome restrictions while protecting the rights of employees.

EQUAL EMPLOYMENT OPPORTUNITY

Delaware's Discrimination in Employment Act (DEA) prohibits employment discrimination on the basis of race, color, age, religion, sex (including pregnancy), sexual orientation, national origin, genetic information, or marital status. DEA is modeled after the federal equal opportunity laws and governs employers employing four or more persons within Delaware. Delaware permits employees who work for employers with four or more employees to sue in Delaware's Superior Court after the exhaustion of administrative remedies, including receipt of a Delaware Right to Sue notice. DEA is the exclusive remedy for state employment discrimination claims. DEA further clarifies that an employee is barred from bringing suit based on the same alleged unlawful discriminatory employment practice in both federal and state court, but rather must select one forum or the other.

Delaware prohibits discrimination against handicapped persons under its Handicapped Persons Employment Protections Act (HPEPA). HPEPA governs employers with 15 or more employees.

HIRING

Medical Exams. Under HPEPA, employers are prohibited from requiring a prospective employee to undergo a medical examination unless an offer of employment conditioned upon passing the exam is outstanding.

Polygraph Exams. Delaware employers are prohibited from requiring employees or prospective employees to take polygraph examinations as a condition of employment or continuation of employment.

Misrepresentations. Employers may be liable for damages as a result of misstatements concerning the terms and conditions of employment made at the time an employee is hired.

Strike Breakers. Delaware statutes make it unlawful for any person not directly involved in a labor strike or lockout to recruit any person for employment or to secure or offer to secure for any person employment when the purpose of such action is to have that person take the place of an employee involved in a labor strike.

TERMS AND CONDITIONS OF EMPLOYMENT

Personnel Files. In Delaware, an employee has a right to inspect his or her personnel file during regular business hours, subject to certain conditions. The

employee may take notes of the contents of the file, but there is no requirement that the employee be permitted to make copies of the contents.

Wages and Hours. Under Delaware's Wage Payment and Collection Act, an employer must pay wages by cash or check on regular paydays at least once each month. An employer may also pay an employee using a paycard if the paycard permits an employee to withdraw the entire amount of his paycheck on his pay date in one transaction that is not subject to a fee. If an employer fails to pay wages without reasonable grounds, the employer may be held liable for liquidated damages in an amount equal to the wages not paid. Withholding of wages is generally prohibited except as specifically provided in the Act. Different rates of pay based on sex are prohibited. Written notification must be given to an employee concerning the rate, time, and place of payment. Employers also have to provide notice of sick leave, benefits, and comparable matters. There are statutory rules governing payment of wages and benefits that cannot be waived by private agreement. Wage and hour records must be kept for three years.

Garnishment of Wages. Delaware law protects 85 percent of an employee's net wages from attachment by his creditors, and only one attachment can be honored at a time. An employee may not be dismissed because his wages have been attached.

Jury Duty. Delaware law prohibits an employer from discharging, threatening to discharge, or otherwise intimidating or coercing an employee because of jury duty. Violation may subject an employer to a fine.

Wire Tapping and Electronic Communications. Generally, Delaware law prohibits monitoring telephone calls absent consent by one party. Similarly, electronic mail may not be intercepted during transmission without the prior consent of one of the parties to the communication. However, no employer, or employer's agent, may monitor or otherwise intercept any telephone conversation or transmission, electronic mail transmission, or internet access or usage of or by an employee unless the employer provides a daily electronic notice or a one-time written notice that is acknowledged by the employee in writing. Violations of these prohibitions are subject to a penalty of \$100 per violation.

Clean Air Act. Delaware prohibits smoking in any indoor enclosed area to which the general public is invited or permitted, including all work places.

Drug and Alcohol Testing. Delaware allows nondiscriminatory, preemployment drug testing for all private employment positions and mandates testing for certain positions, such as nursing home applicants. Generally, for public

employees a balance of privacy rights and governmental concern will be utilized to determine the appropriateness of drug testing during employment. Correctional employees and school bus drivers, however, are subject to random testing. There are no specific statutory limitations on alcohol testing.

Meal Breaks. In general, an employer must allow an employee an unpaid meal break of at least 30 consecutive minutes if the employee works 7.5 or more consecutive hours. However, this may be modified by a collective bargaining agreement or other written employer-employee agreement. There are also statutory exceptions to the general rule for professional education employees working directly with children, instances in which compliance would compromise public safety, and certain enumerated employer-driven requirements.

TERMINATION OF EMPLOYMENT

Delaware follows the traditional rule that a hiring for an indeterminate period is terminable at any time without cause. However, there are some general exceptions. First, the right to discharge at-will employees has been restricted under federal statutes such as Title VII of the Civil Rights Act, the Age Discrimination in Employment Act, and the Family and Medical Leave Act, as well as state statutes such as HPEPA and DEA. Second, if an employee alleges that he was discharged for refusing to violate a federal, state, or local law, or alleges that the discharge was for reporting an employer violation of a federal, state, or local law, the employee may be protected. (See “**Protection For Whistleblowers**” in this chapter below.) Third, an employer may, under certain circumstances, be contractually obligated to the employee through the use of employment handbooks and other similar documents. Fourth, an employer may not discharge an employee for exercising certain statutory rights, such as filing a workers’ compensation claim or refusing to take a polygraph test. Fifth, if an employee alleges that he was discharged for refusing to violate a professional code of conduct governing the employee’s profession, the employee may be protected. Finally, the implied covenant of good faith present in every employment contract, at-will or otherwise, provides an avenue for wrongful termination claims, but those claims are very narrowly limited to violations of public policy, misrepresentation by an employer of a material fact, an employer’s use of superior bargaining power to withhold past compensation, and falsifying records to create fictitious reasons for terminating an employee.

Protection for Whistleblowers. All Delaware employees are protected from being discharged, threatened, or otherwise discriminated against because they report, to a public body or their employer, the violation of a local, state, or fed-

eral law that has occurred or is about to occur. Similarly, an employee cannot be discriminated against because he is requested to participate in an investigation, hearing, or inquiry or because he refuses to violate a federal, state, or local law or regulation.

Notification. There are no statutes in Delaware requiring advance notification of termination of employment.

Wage Payment and Collection. Employers are obligated to pay at the time of termination of employment the employee's wages, which may include bonuses. Payments are required to be made either at the time the employee is terminated or on the next regularly scheduled payday as if the employee had not been terminated. However, an employer has 30 days after termination to make payment of any owed benefit and wage supplements (such as reimbursement for expenses; health, welfare, and retirement benefits; and vacation, separation, or holiday pay).

Unions. Employees have the right to bargain collectively with employers through representatives of their own choosing in order to change wages or other conditions of work. Public employees have the right to organize, but not to strike.

Sale of Business. Delaware law requires that collective bargaining agreements covering employment in Delaware be honored after the sale of a business. Employees can recover wages, liquidated damages, and attorneys' fees.

MISCELLANEOUS

Unemployment Compensation. Generally, an unemployed individual is eligible for unemployment compensation if he (i) has registered at an employment office to work, (ii) has made a claim for benefits, (iii) is able to, available for, and actively seeking work, and (iv) has during his base period been paid wages equal to not less than 36 times his weekly benefit. Disqualifications for benefits include (a) voluntary termination of employment by the employee without good cause attributable to such employment, (b) discharge for just cause, (c) refusal to accept work for which the employee is reasonably fitted, (d) strikes, (e) receipt of unemployment benefits from another governmental entity, (f) fraudulent statements to the Delaware Department of Labor, (g) incarceration, (h) physical inability to work, (i) temporary break in employment because of participation in athletic events, and (j) illegal alien status.

Workers' Compensation Act. The Delaware Industrial Accident Board has jurisdiction over cases arising under the Workers' Compensation Act (WCA).

No wage compensation can be awarded unless the claimed injury arises out of and is sustained in the course of employment and incapacitates an employee from earning full wages for three days. An employee will be compensated beginning on the fourth day of incapacity. However, if the incapacity extends to seven days or more, the employee is entitled to wage compensation from the first day of injury. If an employee is permanently injured, compensation is due to the employee without regard to his earning power, and the employer must also pay for medical services regardless of the period of incapacity. Occupational diseases are also covered under the WCA. It is unlawful for an employer to discriminate or retaliate against an employee because the employee claimed or attempted to claim workers' compensation benefits from the employer.

Specific provisions for total or partial disability from work and schedules for permanent disability, disfigurement, and death benefits are contained in the WCA. A successful employee is entitled to attorneys' fees in the amount of 30 percent of the compensation award or 10 times the average weekly wage in Delaware as announced by the Delaware Secretary of Labor at the time of the award, whichever is less.

The WCA applies to both the employer and employee in any employment where one or more employees are engaged, except as specifically provided otherwise. The WCA does not apply to household workers in a private home or household who earn less than \$750 in cash in any three-month period from a single private home or household, and only applies to farm workers if the employer carries insurance to pay for benefits.

Every employer must be insured by an approved insurer or furnish proof of its ability to pay direct compensation, and must periodically present evidence of such coverage or ability to pay to the Delaware Industrial Accident Board.

Child Labor Law. Generally, a child must be at least 14 years of age to be employed in Delaware. However, the minimum age for some occupations is 16 years or 18 years. The Child Labor Law governs hours of work and requires work certificates before an employer can employ a minor.

Delaware Right to Know Law. "Right to know" legislation has been enacted in Delaware that grants employees exposed to hazardous chemicals in the workplace the right to know to what chemicals they are exposed. The Delaware standards mirror federal OSHA regulations. Employers are required to provide training for employees on how to protect themselves from chemical hazards in the workplace. Penalties for violation may be imposed.

A faint, grayscale background image of the Delaware State Capitol building. The building features a prominent central clock tower with a spire topped by a weather vane. The architecture is classical, with multiple windows and a pedimented roof. The building is reflected in a body of water in the foreground.

CHAPTER SIX

ENVIRONMENTAL LAW

**Delaware's environmental laws balance the interests
of responsible development and the protection of
Delaware's quality of life.**

ENVIRONMENTAL AGENCY AND LAW ENFORCEMENT

The Department of Natural Resources and Environmental Control (DNREC), the primary Delaware environmental agency, issues all major state environmental permits, and develops and enforces state environmental statutes and regulations. DNREC enforces state environmental statutes and regulations through notices of violation, administrative orders, and judicial proceedings for injunctions, civil penalties, and criminal penalties. DNREC also has broad authority to notify parties of environmental violations and to order abatement of such violations. If an imminent environmental hazard is present, DNREC has authority to undertake emergency cleanup itself and recover from the responsible party the costs incurred.

DNREC is also empowered to require independent audits of chronic violators and of facilities where the operator has been found guilty, pled guilty, or pled no contest to any crime involving a violation of environmental standards that resulted in serious physical injury or serious harm to the environment. Additionally, such facilities may be subjected to early submissions of information, and a statement by the chief operating officer that all disclosures were complete and accurate may be required and increased penalties for violation may be imposed.

Environmental permits and zoning approval are required by counties and/or municipalities. Zoning approval generally requires a municipal or county environmental review for commercial or industrial development. The extent of the review depends upon the county or municipality and the size of the proposed development. Projects potentially affecting the Delaware River Basin are subject to approval by the Delaware River Basin Commission. Coastal projects may also require approval under the Coastal Zone Act. (See “**Coastal Zone and Beach Management**” in this chapter below.)

AIR POLLUTION

Delaware has adopted a state implementation plan in conformity with the federal Clean Air Act. A permit must be obtained through DNREC for any equipment, facility, or air contaminant control device that will emit or prevent the emission of an air contaminant. DNREC also administers the Title V permitting program under the federal Clean Air Act pursuant to delegated authority from the federal Environmental Protective Agency (EPA).

COASTAL ZONE AND BEACH MANAGEMENT

DNREC regulates the industrial development of Delaware's coastal zone by implementing the Delaware Coastal Zone Act. New or expanded manufacturing uses in the coastal zone require permits issued by DNREC. Heavy industry and bulk transfer facilities are not allowed in the coastal zone, but other non-manufacturing uses are not affected by this Act. Development on Delaware's beaches is also controlled, and written approval and/or a permit is required for alteration of beaches or dunes and construction on or adjacent to a beach.

HAZARDOUS WASTE

Delaware has enacted the Hazardous Waste Management Act, comparable to the federal Resource Conservation and Recovery Act, that extensively regulates the treatment, storage, and handling of hazardous substances and that provides penalties for violations. Persons generating, transporting, or storing hazardous waste within Delaware must report the action to DNREC, along with specific information about the waste and its storage and disposal. Discharges of hazardous wastes must be promptly reported and abated.

HAZARDOUS SUBSTANCE SITES

The Delaware Hazardous Substance Cleanup Act complements the federal Comprehensive Environmental Response, Compensation and Liability Act (CERCLA) by authorizing cleanup of sites where there has been a release of a hazardous substance. A state "superfund" has been created to fund site cleanup in a manner similar to CERCLA. The state statute applies to a wide spectrum of substances, including substances routinely disposed of by commercial entities. Cost recovery for cleanup actions can be imposed against owners or operators of hazardous substance sites, as well as those persons contributing to a site by owning, sending, or transporting the hazardous substances.

BROWNFIELDS

Voluntary cleanup of contaminated, unoccupied industrial and commercial sites (brownfields) is encouraged by state-funded matching grants for environmental assessment and remediation costs, releases from liability, and tax incentives. (See Chapter Four, "**Taxation – Corporate Income Tax – Credits**" regarding tax credits made available for remediation.)

Delaware has enacted provisions within the Delaware Hazardous Substance Cleanup Act similar to the federal brownfields law (the Small Business Liability

Relief and Brownfields Revitalization Act of 2002) regarding prospective purchasers, innocent landowners, and contiguous properties, although entry into a DNREC-negotiated prospective purchaser agreement is necessary in order to benefit from the liability release. Additionally, in 2004 Delaware enacted a Brownfields Development Program that allows brownfields developers to conduct investigations and/or development activity at a facility with protection from liability for existing contamination by entering into a brownfields development agreement with DNREC.

EXTREMELY HAZARDOUS SUBSTANCES

The handling, use, and storage of toxins, explosives, and flammables/com-bustibles are regulated under the Delaware Extremely Hazardous Substances Risk Management Act. That Act requires registration of facilities involved in extremely hazardous substances, implementation of a risk-management program, documentation and review of equipment and procedures, special training, incident investigation, inspection, and auditing. Delaware's extremely hazardous substances program is similar in scope and content to the comparable federal program, but applies lower thresholds for inclusion of substances in the state reporting scheme.

LAND CONSERVATION AND PRESERVATION

The Delaware Land Protection Act authorizes the protection and conservation of natural and cultural resources as well as the preservation of biological habitats and recreation areas. That Act enables the State to acquire, permanently dedicate, and protect certain land in furtherance of conservation.

SOLID WASTE

Solid waste storage, collection, transportation, processing, transfer, and disposal are extensively regulated by DNREC and the Delaware Solid Waste Authority. Facilities and activities subject to such regulation include sanitary landfills, industrial landfills, dry waste disposal facilities, resource recovery facilities, transfer stations, and special wastes handling. Solid waste facilities are regulated by a permitting procedure that includes a public hearing phase for new sites. The regulations also specify the minimum environmental protection requirements for landfills and other disposal sites.

Infectious waste generated by infectious waste generators must be disposed of in accordance with special procedures. Infectious waste means those wastes that may cause human disease and may be reasonably suspected of harboring

human pathogenic organisms, or may pose a substantial present or potential hazard to human health or the environment when improperly treated, stored, transported, disposed of, or otherwise managed. Included in this definition are blood and other body fluids, human tissue, special cultures, laboratory wastes, discarded pharmaceutical products, and discarded needles and syringes.

OCEAN DUMPING

Any disposal of solid wastes into the ocean waters of Delaware, the Delaware Bay, inland bays, and certain waters of exceptional recreational or ecological significance is prohibited by the Delaware Solid Waste Dumping Elimination Act. Fines are authorized for negligent violators, and imprisonment is authorized for knowing violators.

RECYCLING

Solid Waste Recycling. Delaware is implementing a comprehensive residential and commercial recycling program by municipalities and waste haulers. Under the program, source separated recycling collection services is to be offered to all businesses who provide on-premise sales, and all commercial businesses are expected to actively participate in the program by no later than January 1, 2014. In order to defray the costs of implementing the program, the Delaware Recycling Fund and the Recycling Grants and Low-Interest Program have been established, with funding derived by the conversion of the current bottle deposit to a recycling fee on beverage containers.

Plastics. Plastic bottles and rigid plastic containers distributed, sold, or offered for sale in Delaware must be labeled with a code identifying the resin type used to produce the structure of the container. Delaware also requires that certain retail establishments establish at-store recycling programs for plastic carryout bags, and that these bags be marked with a message encouraging recycling.

State Recycling Effort. Under the Delaware Waste Minimization/Pollution Prevention Act, additional recycling measures have been mandated. Recycling centers for numerous materials have been established throughout the State, and waste minimization has been promoted through various media.

STORAGE TANKS

The Delaware Underground Storage Tank Act was enacted to regulate the installation, operation, and abandonment of underground storage tanks in order to prevent the leakage of petroleum products and other hazardous liquids that results

in degradation of the groundwater. This Act applies to tanks containing petroleum products or any of a number of other substances defined in CERCLA. Excepted from the statute are septic tanks, pipelines, surface pits and lagoons, storm water and wastewater collection systems, and storage tanks in an underground area if the tanks are situated upon or above the surface of the floor.

The Jeffrey Davis Aboveground Storage Tank Act was enacted to regulate the installation, operation, inspection, monitoring, and cleanup responsibilities associated with releases from, and financial responsibilities for, aboveground storage tanks. The requirement to register aboveground tanks and the yearly registration fee schedule varies in accordance with tank size. With a few exceptions, all aboveground storage tanks greater than 250 gallons in capacity are subject to regulation under this Act. Excepted from the statute are heating oil tanks for consumptive use on the premises less than 1,100 gallons in capacity, propane tanks, tanks for use on a farm less than 1,100 gallons in capacity, tanks used solely to store motor fuel or motor oil for noncommercial purposes (also less than 1,100 gallons in capacity), and tanks installed on a temporary basis.

WATER POLLUTION

Delaware has instituted a water permit program consistent with the regulations, guidelines, and priorities of the federal Clean Water Act. DNREC oversees water permit issuance as well as compliance, monitoring, and enforcement under the permit program. Water quality standards and permit procedures are regulated by the State's Regulations Governing Control of Water Pollution and Surface Water Quality Standards. DNREC has also issued Total Maximum Daily Load regulations for many of the surface waters in the State that are not attaining applicable surface water quality standards. Water wells, underground injection control, storm water discharges associated with industrial activity, operation of wastewater treatment facilities, and pollution of water by oil discharge are all separately regulated by DNREC.

WETLANDS

The Delaware Wetlands Act was enacted to prevent the loss of state wetlands to unregulated activities. This Act sets forth a permitting system designed to preserve remaining Delaware wetlands. Wetlands areas have been mapped, and activities such as construction, draining, and dredging in the wetlands may only be commenced after approval by DNREC. DNREC, the EPA, and the U.S. Army Corps of Engineers are all involved in the review of proposed projects in wetlands areas.

SPILL REPORTING

State law mandates that any person who causes or contributes to the discharge of an air contaminant into the air, a pollutant into surface water or groundwater or onto land, or the disposal of solid waste in excess of any reportable quantity must report such an incident to DNREC at the earliest opportunity after the discharge has occurred. Under certain circumstances, notification of the local Emergency Planning Commission is also required. Permits issued to operating facilities typically contain additional and more extensive reporting requirements. These requirements are in addition to any reporting requirements under federal law.

ENERGY

Delaware has enacted the Delaware Energy Act establishing a State Energy Office (SEO) within DNREC. The purpose of SEO is, in part, to encourage and promote energy conservation and the use of renewable and alternative energy technologies, and to administer the monies in the Green Energy Fund. The monies in the Green Energy Fund are administered as grants and loans for the development, promotion, and support of renewable or alternative energy technology in the State. Delaware has also created a Sustainable Energy Utility to develop customer-sited renewable energy generation and end-user energy efficiency.

CHAPTER SEVEN

INTELLECTUAL PROPERTY

**State rules supplement federal protection
of intellectual property.**

PATENTS

The federal patent system allows a patent to issue for inventions that are useful, novel, and nonobvious. A patent allows the inventor to exclude others from using, making, and selling the invention for a limited time in exchange for full disclosure of the invention. Any state statute that purports to give an inventor extended protection for his or her invention runs counter to the federal patent policy and would likely be held invalid. Delaware has no statute that undertakes to govern patentable inventions.

The United States District Court for the District of Delaware sitting in Wilmington has developed a national reputation for the adjudication of patent disputes. It has adopted procedures and orders for the prompt resolution of such disputes. (See Chapter Eight, “**Dispute Resolution – United States District Court for the District of Delaware – Intellectual Property Litigation.**”)

State law applies in a patent context when the licensing of a patent is involved. In Delaware, fundamental rules of contract construction apply equally to the construction of patent licenses. In granting a license, the patentee can retain any of the rights to make, sell, and use the invention, while conveying others.

CERTAIN TECHNOLOGY AND BUSINESS DISPUTES

The Delaware Court of Chancery has statutory jurisdiction over actions involving certain technology disputes. That court is also authorized to conduct confidential mediation of many types of complex business disputes. These mechanisms provide parties access to a sophisticated and efficient judiciary for effective dispute resolution.

The Court of Chancery has jurisdiction to hear and determine “technology disputes” that meet certain criteria. A technology dispute is defined as a dispute arising out of an agreement and primarily relating to: (i) the purchase or lease of computer hardware; (ii) the development, use, licensing, or transfer of computer software; (iii) technology of a complex or scientific nature (*e.g.*, biological, pharmaceutical, or agricultural) that has commercial value or the intellectual property rights pertaining thereto; (iv) the creation or operation of internet websites; (v) the rights or electronic access to electronic, digital, or similar information; or (vi) the support or maintenance of the above. The law provides that the Court of Chancery shall interpret the term “technology dispute” liberally to provide an expeditious and expert forum for the handling of technology disputes. The Court of Chancery has established rules and set filing

fees and other costs for the processing of technology disputes. Neither punitive damages nor a jury trial is available for a technology dispute presented for determination in the Court of Chancery.

The Court of Chancery also has jurisdiction to mediate and arbitrate business disputes, including technology disputes, if the parties request that a member of the Court of Chancery act as a mediator or arbitrator. The Court of Chancery obtains jurisdiction when the parties have consented by agreement or stipulation to the mediation or arbitration, at least one party is a Delaware business entity, no party is a “consumer,” and, in the case of disputes involving solely a claim for monetary damages, the amount in controversy is not less than \$1 million. These judicial mediation and arbitration proceedings are considered confidential and are not a matter of public record. The statute allows the Court of Chancery to define those types of cases that are eligible for submission as a business dispute, with the statute giving the court broad rule-making authority to effectuate the statute’s intent. (For more information on these dispute resolution mechanisms, see Chapter Eight, “**Dispute Resolution – State Court System – Trial Courts – The Court of Chancery.**”)

TRADEMARKS AND SERVICE MARKS

The Delaware Trademark Act, derived from the Model State Trademark Act, generally provides that any person who adopts and uses a distinctive trademark or service mark in Delaware may register the mark with the Delaware Secretary of State and obtain legal protection of that mark. Registration of a mark may be limited by the preexisting rights of another.

The Delaware Trademark Act applies to any mark not immoral; deceptive; scandalous; disparaging; containing the flag, coat of arms or other insignia of a municipality, state, or nation; containing the name, signature, or portrait of any person without his consent; primarily geographically descriptive; primarily merely a surname; or resembling a mark previously registered or used.

Registration of a mark is obtained by application to the Delaware Secretary of State. Information required includes the type of goods or services for which the mark will be used, the class in which such goods or services fall, the manner in which the mark will be used, the date when the mark was first used anywhere, the date when the mark was first used in Delaware by the applicant or his predecessor in business, and a signed statement by the applicant stating that he is the owner of the mark and that no other person has the right to use the mark. The application must be accompanied by a specimen or facsimile of the mark

in duplicate and a filing fee of \$25 payable to the Secretary of State. A certificate of registration will be issued upon payment of an additional \$10 fee. The duration of a registered trademark or service mark is 10 years (renewable for successive periods of 10 years, upon application filed within six months before the expiration of the prior term, for a fee of \$25).

Registration of a trademark or service mark yields protection against any usage or copying by others without consent. The Delaware Trademark Act authorizes the use of injunctions to protect against infringement, as well as court-ordered destruction of counterfeit marks. An infringing party may be liable for profits derived from the mark and damages suffered by the registrant.

The Delaware Trademark Act does not contain a provision for the reservation of a mark with intent to use it in the future. Additionally, the required distinctiveness of a mark is not necessarily established by proof of continuous use of the mark for any specified period of time preceding registration.

The Delaware Trademark Act also contains an anti-dilution provision. This protects against the likelihood of injury to business reputation or dilution of the quality of a registered mark, notwithstanding the absence of competition between the parties or the absence of confusion as to the source of goods or services.

COPYRIGHTS

Delaware has not enacted a state copyright law or any other law protecting original works of authorship. The federal Copyright Act generally subjects state laws to federal preemption. However, Delaware courts recognize a state common law action for unfair competition. For original works of authorship, this could affect the “passing off” situation—where a person attempts to sell his goods under the pretense that they are someone else’s original goods.

TRADE SECRETS

Delaware has adopted the Uniform Trade Secrets Act. The Delaware Act protects the ownership of trade secrets, defined as information, including a formula, pattern, compilation, program, device, method, technique, or process, that:

- (a) Derives independent economic value...from not being generally known to, and not readily ascertainable by proper means by, other persons...; and
- (b) Is the subject of efforts that are reasonable under the circumstances to maintain its secrecy.

An action for misappropriation of a trade secret must be brought within three years after the misappropriation has been or should have been discovered by the exercise of reasonable diligence. The Delaware Act authorizes injunctive relief for actual or threatened misappropriation. Complainants also may seek monetary damages for actual loss and unjust enrichment, or a reasonable royalty in lieu of other measures of monetary damages. Exemplary damages are available for willful and malicious misappropriation in the amount of twice the actual damages. The prevailing party may recover attorneys' fees for claims and motions made in bad faith and for those misappropriations deemed to be willful and malicious. Delaware courts will take reasonable precautions to protect under the Delaware Act trade secrets that are the subject of litigation.

USE OF DELAWARE INVESTMENT COMPANIES TO HOLD INTELLECTUAL PROPERTY

As described in Chapter Four, “**Delaware Taxation – Corporate Income Tax – Delaware Investment Companies,**” state law provides an exemption from Delaware corporate income tax and gross receipts tax for corporations whose activities within Delaware are limited to the maintenance and management of their intangible investments and the collection and distribution of the income from such investments. These corporations, known as Delaware investment companies, have often been used to hold intellectual property as part of a plan to reduce overall state income taxes. Royalty fees or license payments received by a Delaware investment company for the use of its intellectual property under a license arrangement not only can qualify for exemption from Delaware tax but also may generate a state income tax deduction for the licensee in its home state.

The Delaware Division of Revenue has issued rulings recognizing the Delaware tax-exempt status of Delaware investment companies holding such intellectual property assets as patents, patent applications, inventions, know-how, trademarks, service marks, trade names, copyrights, trade secrets, and mask works. As a consequence, many companies have established Delaware investment companies to hold their intellectual property assets and thereby achieve significant state income tax savings.

CHAPTER EIGHT

DISPUTE RESOLUTION

Delaware's efficient courts are nationally known for expertise in corporate, business, and commercial law.

STATE COURT SYSTEM

Delaware has an efficient and professional court system that is nationally and internationally prominent in a number of areas, particularly corporate, business, and commercial law. Judges are appointed, not elected, thus insulating the judiciary from undue political and special-interest influence. Delaware judges are specifically prohibited from engaging in political campaigns and other political activity.

The structure of the Delaware court system lends itself to the prompt and expert disposition of cases. There is no intermediate court of appeals between the trial-level courts of general jurisdiction and the highest court of appeals, facilitating prompt final adjudication of disputes. The jurisdiction of the trial-level courts is divided so that certain types of business disputes are heard by sophisticated judges rather than juries composed of lay citizens, facilitating predictability and expertise in the disposition of cases.

Delaware's judicial system and its widely recognized high level of judicial expertise and legal stability contribute to Delaware's preeminence as the leading jurisdiction in which to incorporate and as a favorable location to conduct business. In 2010, for the eighth year in a row, a U.S. Chamber of Commerce study ranked Delaware first in providing a legal climate that attracts business.

OVERVIEW OF STATE COURT SYSTEM

The Delaware judicial system consists of the Supreme Court, Court of Chancery, Superior Court, Family Court, Court of Common Pleas, and Justice of the Peace Courts. The Delaware Constitution of 1897 also established a Court on the Judiciary with power to censure, remove, or retire judicial officers for misconduct or failure to perform duties. Various municipalities operate Alderman's Courts.

The Supreme Court is the highest court in the State. The Court of Chancery and the Superior Court are the trial-level courts of general jurisdiction, appeals from which are directly to the Supreme Court. The Family Court exercises jurisdiction over matters of domestic relations and most offenses involving juveniles. The remaining courts are courts of limited jurisdiction, as described below.

THE SUPREME COURT

The Supreme Court is the highest appellate court in Delaware and has final appellate jurisdiction in civil appeals from final judgments, discre-

tionary appellate jurisdiction over interlocutory appeals in civil cases, and final appellate jurisdiction in criminal appeals where the sentence exceeds certain minimums. The Supreme Court has additional jurisdiction with respect to writs of prohibition, *quo warranto*, *certiorari*, and *mandamus*.

The Supreme Court consists of five justices, one of whom is the chief justice. The chief justice is responsible for the administration of all courts of the State. Justices of the Supreme Court are appointed by the Governor, subject to the advice and consent of the Delaware Senate, for 12-year terms. Justices must be citizens of Delaware learned in the law.

The Supreme Court, along with the Court of Chancery (described below), is nationally and internationally regarded as having particular expertise in issues of corporate law, including mergers and acquisitions, shareholder rights, fiduciary relations, and director liability. Its decisions frequently have broad national importance and often influence the jurisprudence in other states on these subjects. On average, appeals to the Supreme Court are resolved, from date of filing to final disposition, in approximately 180 days. The court is accustomed to hearing expedited appeals where circumstances warrant, and such appeals are typically resolved in a much shorter time—sometimes within days.

The Supreme Court has additional constitutional jurisdiction to hear and determine questions of law certified to it by other Delaware courts, the Supreme Court of the United States, courts of appeal or district courts of the United States, the United States Securities and Exchange Commission, or the highest appellate court of any other state. This jurisdiction has been invoked to determine issues of Delaware corporate law that arise in cases in litigation in other, non-Delaware, courts.

In addition to its appellate function, the Supreme Court operates through a number of separate agencies in its administration of the lower courts and the Delaware bar. These include the Board on Professional Responsibility and the Office of Disciplinary Counsel, which enforce Delaware's ethical rules governing the conduct of lawyers; the Board on the Unauthorized Practice of Law, which ensures that law is practiced only by duly admitted professionals; the Board of Bar Examiners, which tests qualification for admission to the bar; the Commission on Continuing Legal Education, which administers the continuing legal education requirements applicable to members of the bar; and the Supreme Court Rules Committee, which monitors and, where appropriate, recommends changes in the practice rules of the Supreme Court.

TRIAL COURTS

The lower courts of Delaware are divided into courts of general jurisdiction and courts of limited jurisdiction. With respect to the trial courts of general jurisdiction, Delaware is one of the few states that has maintained the historical separation of law and equity that existed in English jurisprudence at the time of the American Revolution. This separation of jurisdiction has had a substantial and favorable effect on the development and stability of corporate and business law in Delaware and, because of the influence of Delaware law, across the United States.

The Court of Chancery. The Court of Chancery has jurisdiction to hear and determine all causes and matters in equity and to grant traditional equitable remedies such as injunctions, reformation, rescission, specific performance, accountings, and the like. The general equity jurisdiction of the Court of Chancery derives from the jurisdiction of the English High Court of Chancery as it existed at the time of the separation of the American colonies from the English Crown, but its jurisdiction has been substantially supplemented by statutory grants of jurisdiction over specific subject matters.

The Court of Chancery also has limited appellate jurisdiction, hearing appeals from specified state agencies, such as the Securities Commissioner. Appeals from the decisions of the Court of Chancery are directly to the Delaware Supreme Court.

The Court of Chancery consists of one chancellor and four vice chancellors. The chancellor and vice chancellors are appointed by the Governor, subject to the advice and consent of the Senate, for 12-year terms. In view of the particular expertise expected of the Court of Chancery in corporate and other fiduciary matters, the chancellor and vice chancellors historically have been experienced and sophisticated practitioners familiar with these areas at the time of their selection.

Litigation in the Court of Chancery. Litigation in the Court of Chancery consists largely of corporate governance, merger and acquisition, fiduciary duty, statutory appraisal, and other corporate matters; partnership matters; trusts, estates, and other fiduciary, commercial, and contractual matters; and real estate disputes. The Court of Chancery hears cases without a jury and has no jurisdiction to award punitive damages. It is the leading tribunal in the United States on issues of corporate governance and fiduciary responsibility.

The internationally recognized expertise of the Court of Chancery in resolving complex corporate disputes was established in the early part of the 20th

century and continues unabated today. The Court of Chancery is not subject to the backlogs or the distractions of criminal and tort cases that affect the litigation process in other jurisdictions. This results in part from its limited subject matter jurisdiction, which promotes specialization and expertise in its judges and the lawyers who practice before it.

The structure of the Court of Chancery and the nature of practice before it lend themselves to expeditious proceedings and prompt, expert resolution of cases, particularly where injunctive relief is sought. The Court of Chancery's procedural rules do not impose formalistic schedules and procedures, but allow the court and the parties to conduct litigation on a schedule suitable to the needs of the individual case. The court's discovery and evidence rules are generally consistent with, although not identical to, rules applied in federal courts.

Expedited Proceedings in the Court of Chancery. Expedited proceedings are available for almost any suit brought in the Court of Chancery in which such treatment is shown to be necessary. Typically, the party seeking expedited proceedings will need to show good cause as to why the litigation schedule should be expedited or summary in nature.

The General Corporation Law of the State of Delaware contains certain provisions that confer jurisdiction on the Court of Chancery to resolve specific corporate disputes and that provide mechanisms for enforcement of specific corporate rights. Proceedings arising from some of these provisions are explicitly designated as summary proceedings, and others have been consistently treated as such notwithstanding the absence of explicit language in the statute.

Procedures for presenting a request for expedited proceedings, and the procedures for conducting the litigation once the matter is expedited, are not specifically set forth in the Court of Chancery Rules. Rather, when the need for expedited treatment arises, one or more of the parties may request the court to expedite the case. If the court decides that the matter should be expedited, it will enter an order so providing, which may include fixing a specific time for the filing of any responsive pleadings or motions, authorizing and setting dates for accelerated discovery, scheduling the dates for any prehearing or pretrial briefing, and setting hearing or trial dates. Such expedition and the prompt resolution of disputes it implies have been hallmarks of the Court of Chancery and have contributed to the court's attractiveness as a forum for resolving disputes.

Additional Dispute Resolution Mechanisms in the Court of Chancery. To enhance the Court of Chancery's status as the preeminent forum for the resolution of complex commercial disputes, the Court of Chancery also has been

granted power to mediate and arbitrate complex corporate and commercial disputes and to adjudicate certain technology disputes, including disputes involving solely claims for money damages (which would otherwise be excluded from the court's traditional equity jurisdiction). The availability of "mediation only" and arbitration procedures in the Court of Chancery for these types of business disputes is intended to facilitate voluntary and confidential resolution of complex business disputes between parties in an efficient and expert forum.

The Court of Chancery has power to conduct confidential mediation of business disputes when the parties have consented to such mediation by agreement or stipulation, at least one party is a business entity formed or organized in Delaware or having its principal place of business in Delaware, no party is a consumer, and, if the dispute involves only money damages, the amount in controversy exceeds \$1 million. The mediation proceeding does not need to relate to or arise from any preexisting litigation in the court, but may be commenced on a stand-alone, mediation-only basis.

Unusual for a proceeding in a public court, the mediation is entirely confidential. The mediation petition and supporting documents are confidential and are not kept on the public docket as public documents, and mediation conferences are by rule private proceedings such that only the parties, their counsel, and the mediator may attend, unless otherwise agreed among them.

The mediator in a Court of Chancery "mediation only" proceeding will be the chancellor, one of the four vice chancellors, or a master sitting permanently in Chancery, ensuring that the mediating parties will have the advantage of a sophisticated mediator. If the mediation succeeds, the parties' agreement is to be memorialized in an agreement signed by them and by the judicial mediator; if the mediation is unsuccessful, the mediator is ineligible to adjudicate any subsequent litigation that may arise from the issues mediated.

The Court of Chancery also has power to conduct confidential arbitration of business disputes that meet criteria similar to those for which it can provide confidential mediation. As in the case of "mediation only" proceedings, Court of Chancery arbitration proceedings are private and confidential proceedings. A Court of Chancery arbitration proceeding will result in an arbitral award that is entered as a judgment or decree of the court.

Any application to vacate, stay, or enforce an order of the Court of Chancery issued in an arbitration proceeding is filed in the Delaware Supreme Court, which will exercise its authority in such proceeding in conformity with the Federal Arbitration Act and general legal and equitable principles not inconsis-

tent with that Act. The parties may stipulate in advance that any decision of the Court of Chancery shall be final and binding and not subject to appeal.

Both mediation and arbitration proceedings in the Court of Chancery are intended to proceed more expeditiously than similar nonjudicial proceedings. The mediation rules provide that the mediation conference will generally occur no later than 60 days after filing of the petition commencing the mediation, while the arbitration rules provide that the arbitration hearing generally will occur no later than 90 days after filing of the petition for arbitration.

Technology Disputes. The Court of Chancery also has statutory, nonexclusive jurisdiction to hear and determine (and to mediate, if so agreed) technology disputes that otherwise might be outside the court's traditional equitable jurisdiction. Technology disputes are disputes arising out of an agreement and relating primarily to the purchase or lease of computer hardware; the development, use, licensing, or transfer of computer software; information, biological, pharmaceutical, agricultural, or other technology of a complex or scientific nature that has commercial value, or the intellectual property rights pertaining thereto; the creation or operation of internet websites; rights or electronic access to electronic, digital, or similar information; or support or maintenance of the foregoing.

To be within the Court of Chancery's jurisdiction to mediate or adjudicate a technology dispute, the parties must have consented to the court's jurisdiction by agreement or stipulation, at least one party must be a business entity formed or organized under Delaware law or having its principal place of business in Delaware, no party may be a consumer, and, in the case of claims involving only money damages, the amount in dispute must exceed \$1 million. Neither punitive damages nor a jury trial are available for a technology dispute adjudicated under authority of this statutory grant of jurisdiction.

The authority of the Court of Chancery regarding a technology dispute may be fixed by the parties, who may, by agreement, provide for the court to mediate the dispute only, to mediate the dispute and, if that fails, to adjudicate the dispute, or to adjudicate the dispute. The Court of Chancery's rules relating to mediation of business disputes apply to mediation of technology disputes, and its litigation rules apply to adjudication of technology disputes.

The Superior Court. The Superior Court is the State's trial-level court of general jurisdiction, hearing matters of law as opposed to equity matters, which are heard by the Court of Chancery. The Superior Court consists of 18 judges, one of whom is the president judge. Superior Court judges are appointed by the Governor, subject to the advice and consent of the Senate, for 12-year terms.

The judges are drawn from a wide background of experience in the legal profession, reflecting the varied nature of the cases that come before the Superior Court. The judges are divided between those who primarily hear civil cases and those who primarily hear criminal cases. Civil cases are assigned to a single judge for the duration of the case.

The Superior Court exercises appellate jurisdiction in appeals from the Court of Common Pleas, Family Court (adult criminal cases), and more than 50 administrative agencies. These appeals are heard on the record, while appeals to the Superior Court from the Alderman's Courts and Justice of the Peace Courts are heard as trials de novo. Appeals from the decisions of the Superior Court may be taken on the record to the Supreme Court.

Litigation in the Superior Court. The Superior Court has statewide jurisdiction over civil and criminal cases and hears, for example, cases of personal injury, libel and slander, contract claims, professional malpractice, products liability, and property cases such as mechanics' liens, condemnations, mortgage foreclosures, and certain landlord-tenant disputes. The Superior Court's authority to award damages is not subject to a monetary maximum, and trial by jury is available as at common law. The Superior Court has exclusive criminal jurisdiction over felonies and most drug offenses, except those heard in Family Court involving minors. The Superior Court also has jurisdiction over involuntary commitment proceedings. The Superior Court's procedural, discovery, and evidence rules are similar, but not identical, to those applied in federal court.

Most civil cases must preliminarily be submitted to compulsory alternative dispute resolution (ADR), the format of which is to be agreed upon by the parties. Such ADR may include nonbinding arbitration, binding arbitration, mediation, or neutral case assessment. If the parties are unable to agree on the format of ADR, the default shall be mediation unless otherwise ordered by the court. Regardless of the form of ADR, the ADR practitioner may not be called as a witness in any aspect of the litigation, or in any proceeding relating to the litigation in which the ADR practitioner served, unless ordered by the court. In addition, ADR practitioners, when serving as arbitrator, mediator, or neutral assessor, are immune from liability for, or resulting from, any act or omission done or made while engaged in ADR, unless the act or omission was performed in bad faith or with malicious intent. Each ADR practitioner is bound by a confidentiality agreement signed by the parties and the ADR practitioner as a part of the ADR.

Superior Court Procedures for Complex Commercial Cases. A Complex Commercial Litigation Division (CCLD) has been created in the Superior Court to promote the efficient and expeditious handling of complex commercial and business cases in the New Castle County Superior Court. Any case that includes a claim asserted by any party with an amount in controversy of \$1 million or more, or involves an exclusive choice of court agreement or a judgment resulting from an exclusive choice of court agreement, or is so designated by the president judge of the Superior Court, qualifies for assignment to the CCLD. Excluded cases include any case containing a claim for personal, physical, or mental injury; mortgage foreclosure actions; mechanics' lien actions; condemnation proceedings; and any case involving an exclusive choice of court agreement where a party to the agreement is an individual acting primarily for personal, family, or household purposes or where the agreement relates to an individual or collective contract of employment.

Administration of the CCLD is governed by certain CCLD-specific principles. Unless specially assigned by the president judge, a case identified as a qualifying case is assigned, on a rotating basis, to a judge on a special CCLD panel. The panel judges are appointed by the president judge from among the Superior Court judges, and each judge on the panel serves a three-year term unless replaced by the president judge. Judges assigned to the panel collaborate to promote uniformity in case management. If a case is assigned initially to a judge of the court under another case category and it is subsequently identified as a qualifying case, it is reassigned to a CCLD panel judge.

The assigned panel judge will hold an early Rule 16 scheduling conference after all responsive pleadings have been filed. At the conference, the parties meet and confer with the panel judge concerning the progression of the case through trial and preparation of a case management order. The case management order establishes a procedure for handling discovery disputes and dispositive motions, which may include the handling of such disputes by the panel judge or a particular commissioner or appointed special master, require early mandatory disclosures such as those contemplated by Federal Rule of Civil Procedure 26(a), establish procedures for electronic discovery and other matters relevant to the case (e.g., appropriate protective orders and alternative dispute resolution procedures), and address other matters set forth in Rule 16 and any other matters appropriate in the circumstances of the case. Firm pretrial and prompt trial dates are established and will not be continued due to scheduling conflicts with other civil cases. Trials are scheduled during the panel judge's scheduled civil rotation

on the soonest practicable date, given the pretrial complexities of the case, and are given priority as among the panel judge's other trial assignments.

Prior to trial, the court will set procedures for the conduct of the trial as a bench trial, should the parties agree to a bench trial, including procedures to streamline the presentation of evidence, to present legal issues in pretrial and/or post-trial briefs, to ensure prompt and effective post-trial decisions on the merits, and to establish appropriate special procedures for the selection of the jury and the conduct of the trial before a jury should the parties elect a jury trial.

Summary Superior Court Proceedings for Major Commercial Disputes.

The Superior Court has rules and procedures designed to allow parties to agree in advance for major commercial litigation to be resolved expeditiously and cost-effectively in a special, expedited judicial process. Procedures in these cases are greatly simplified, discovery is curtailed, there are no jury trials or punitive damages, and long delays are effectively precluded. Summary proceedings are intended to alleviate the delays and risks of jury trials encountered by businesses in major commercial litigation, while assuring litigants a neutral and sophisticated dispute resolution forum.

There are several criteria for an action to be eligible for treatment as a summary proceeding in the Superior Court. There must be at least \$100,000 in controversy as to one party, although upon application of the parties the court may in its discretion agree to apply the summary proceedings rules to actions involving lesser amounts. One party must be a Delaware citizen, corporation, or other business entity. All of the parties to a summary proceeding must agree to the matter being tried as such. This agreement may preexist the dispute, such as by inserting a provision in an agreement that any dispute arising under the agreement will be litigated in the Delaware Superior Court as a summary proceeding. In addition, the nature of the claim must be contractual or commercial; claims asserting personal, physical, or mental injury may not be brought as summary proceedings. Neither punitive damages nor a jury trial is available in a summary proceeding.

Where all parties consent in advance of the filing of a complaint to the treatment of the litigation as a summary proceeding, the action may be filed as such. The complaint must contain a statement of the amount in controversy, that one of the parties is a Delaware citizen or entity, and that the defendant has agreed to submit to the court's jurisdiction for summary proceedings. Alternatively, an action previously filed in Superior Court or in any other court may be trans-

ferred to the Superior Court and converted into a summary proceeding if the action could have been brought initially as a summary proceeding.

One of the principal features of summary proceedings is the availability of only limited discovery. Each party is limited to 10 interrogatories and requests for admission, and depositions are limited to the other side's identified witnesses and affiants and four other persons. The summary proceedings rules require certain mandatory discovery. Litigants are required at an early stage of the proceedings to identify the documents they intend to rely upon at trial, the witnesses they intend to call at trial, and all persons consulted in preparation of the complaint or answer. The summary proceedings rules contain express discovery cut-offs: all depositions must be completed within 120 days from filing of the last answer, all fact discovery must be completed within 180 days from filing of the last answer, and all expert discovery must be completed within 60 days after completion of the fact discovery.

Where litigants choose to employ live witnesses at trial, trial is to commence within 30 to 60 days after the close of discovery and is to be completed within 5 trial days. The parties simultaneously file post-trial briefs. If the parties elect to forego witnesses at trial and instead submit briefs upon which the court will make factual findings, trial consists of oral argument held within one week from the close of briefing. In either case, the court's decision is to be rendered 30 days after the trial or 30 days after oral argument, if oral argument occurs, so that final decisions should be rendered not more than 10 months to a year from the filing of the complaint.

Cases treated as summary proceedings may be appealed directly to the Delaware Supreme Court. No interlocutory appeals may be taken in a case being treated as a summary proceeding. Appeals from cases tried as summary proceedings are expedited.

Family Court. The Family Court is a unified statewide court having jurisdiction over matters of juvenile delinquency, child neglect, dependency, child abuse, adult misdemeanor crimes against juveniles, child and spousal support, paternity, custody and visitation, adoptions, terminations of parental rights, divorces and annulments, property divisions, specific performance of separation agreements, guardianships over minors, and intra-family misdemeanor crimes. The Family Court does not have jurisdiction over adults charged with felonies or minors charged with first- or second-degree murder, rape, or kidnapping. Appeals are to the Delaware Supreme Court, with the exception of adult criminal cases, which are appealed to the Superior Court. Family Court

judges are appointed by the Governor, subject to the advice and consent of the Senate, for 12-year terms.

The Family Court provides for arbitration in certain circumstances. Family Court arbitration is an informal proceeding in which a trained arbitration officer attempts to resolve juvenile delinquency cases involving minor charges and selected adult misdemeanor cases. In this nonadversarial proceeding, the arbitration officer, after reviewing the charges and listening to the respective positions of the parties, issues a disposition specifying conditions, such as probation or restitution, that must be met by the defendant within 90 days. A defendant who fulfills the dispositional terms does not have a formal finding of guilt. The complainant or defendant may request a review of the disposition by a deputy attorney general within 10 days of the arbitration proceeding.

Court of Common Pleas. The Court of Common Pleas has statewide jurisdiction in civil actions where the amount involved in the complaint does not exceed \$50,000. However, there is no limitation on the amount involved in counterclaims. All civil cases in the Court of Common Pleas are heard without a jury. Most civil cases must be submitted to compulsory alternative dispute resolution, similar to the procedure in the Superior Court. The form of alternative dispute resolution can be selected by the parties, including, but not limited to, mediation, binding arbitration, or nonbinding arbitration.

The Court of Common Pleas has criminal jurisdiction over all criminal misdemeanors occurring in the State, other than drug-related cases and misdemeanors occurring in the City of Wilmington. Jury trials in criminal cases are available. The Court of Common Pleas consists of nine judges, appointed by the Governor for 12-year terms, subject to the advice and consent of the Senate.

Justice of the Peace Courts. The Justice of the Peace Courts have jurisdiction over civil cases in which the amount in controversy does not exceed \$15,000. Justice of the Peace Courts are authorized to hear certain misdemeanors and most motor vehicle cases (excluding felonies) and may act as committing magistrates for all crimes. Civil appeals may be taken de novo to the Court of Common Pleas. The subject matter jurisdiction of the Justice of the Peace Courts is shared with the Court of Common Pleas.

Justices of the peace are nominated by the Governor and confirmed by the Senate for terms of four years. In addition to the justices of the peace, the Governor nominates a chief magistrate, subject to Senate confirmation.

Alderman's Courts. Alderman's Courts are authorized by the town charters of certain municipalities and have jurisdiction only within their own town limits. There are 11 active Alderman's or Mayor's Courts. When a town is without a court or an alderman for any period of time, its cases are transferred to the nearest Justice of the Peace Court. The selection, number, tenure, and qualifications of aldermen are determined by the towns themselves. A few aldermen serve full-time, but most are part-time judges.

The jurisdiction of an Alderman's Court is limited to misdemeanors, traffic offenses, parking violations, and minor civil matters. The specific jurisdiction of each court varies with the town charter (which is approved by the State General Assembly). Appeals are taken de novo to the Superior Court.

NONJUDICIAL ALTERNATIVE DISPUTE RESOLUTION

In addition to the judicial alternative dispute resolution mechanisms provided for under the rules of the Court of Chancery and the Superior Court, Delaware favors additional nonjudicial forms of alternative dispute resolution, including private arbitration, mediation, and neutral assessment.

Arbitration. Arbitration is a process by which a neutral arbitrator hears both sides of a controversy and renders a fair decision based on the facts and the law. The parties can agree that the arbitration will be binding or nonbinding. If the parties stipulate in writing that the decision is binding, upon the arbitrator's decision the case will be closed and removed from the docket.

The arbitration is conducted before one or more arbitrators as selected by the parties and based upon the size and needs of the case. All aspects of the arbitration are confidential. The parties and the arbitrator may disclose the existence, content, or results of the arbitration only in accordance with the rules of the court or applicable professional standards.

Delaware has adopted the Uniform Arbitration Act. Under that Act, the Delaware Court of Chancery has jurisdiction to enforce a written agreement to submit to arbitration and to enter judgment on an award arising from such an agreement. In enforcing the agreement or entering judgment on an award, the Court of Chancery does not pass upon the merits of the dispute underlying the arbitration agreement. A party seeking to compel an arbitration pursuant to a written agreement may file a complaint in the Court of Chancery.

Mediation. Mediation is a process by which a mediator facilitates the parties in reaching a mutually acceptable resolution of a controversy. Generally, the mediator is selected by the parties or, if the parties cannot agree, by the court. The mediator conducts the mediation as he or she determines, with the agreement of the parties. Ordinarily, the parties are required to submit a confidential mediation statement to the mediator, setting forth their claims and defenses in detail. At the mediation, the parties discuss their differences in good faith and attempt, with the mediator's assistance, to reach an amicable resolution of the dispute. For purposes of confidentiality, the mediation includes all contacts between the mediator and any party or parties until a resolution is agreed to, the parties discharge the mediator, or the mediator determines that the parties cannot agree. Similarly, the mediator may not testify for either party in any later proceeding relating to the dispute, and the mediation proceedings shall not be recorded or transcribed.

As with ADR in the other state courts, any communication during mediation or in connection with the mediator or a party to any person if made at a mediation conference is confidential. Information that is disclosed to the mediator by a party or counsel during the mediation session, including any written submissions, is not disclosed to the other party without consent. All mediation proceedings are confidential, are not admissible as evidence in other proceedings, and may not be recorded without prior consent of the parties and the mediator. If a resolution cannot be reached, the mediator will officially terminate the mediation conference without prejudice to any party.

Neutral Assessment. Neutral assessment is a technique in which an impartial party, a neutral assessor, examines the evidence in the case, listens to the parties' positions, and then gives the parties his or her evaluation of the case. The process enhances communication between the parties about their claims and evidence, provides an assessment of the merits of the case by the neutral expert, helps to identify and clarify the central issues in dispute, and assists with discovery and motion planning or with an informal exchange of key information. This dispute resolution process has been successfully used to seek assessments, evaluations, and possible settlements in cases headed for arbitration.

In most cases, the parties are each required to serve upon the neutral assessor a hearing statement, along with any supporting exhibits for the neutral assessor to review. At the hearing, each party presents its evidence and arguments informally to the neutral assessor. The assessor provides an evaluation of the

case to the parties, including an estimate of the likelihood of liability, the dollar range of damages, and an assessment of the strengths and weaknesses of each party's case. The neutral assessor provides reasoning to support these assessments, identifies areas of agreement, clarifies and focuses issues, and encourages the parties to reach a settlement.

UNITED STATES DISTRICT COURT FOR THE DISTRICT OF DELAWARE

The United States District Court for the District of Delaware has federal jurisdiction over the entire State of Delaware. The court sits in Wilmington. The court is notable for hearing and trying a large number of patent and other complex commercial disputes. The District Court has limited original and broad appellate jurisdiction over bankruptcy disputes heard in the Delaware Bankruptcy Court. Appeals from the District Court are taken to the United States Court of Appeals for the Third Circuit or, in some cases, the Federal Circuit.

Intellectual Property Litigation. The District of Delaware has become one of the preferred venues for original adjudication of intellectual property disputes, particularly in the patents area. The judges of the court have procedures and rules in place for handling patent litigation and frequently try more patent cases per judge than any other district in the country. The types of patent cases handled by the court vary, although a recent emphasis is on pharmaceutical and computer patents. After the judges review the initial pleadings, a scheduling conference is held that typically governs the progress of the remainder of the case. Affirmed trial dates provide certainty to the parties that the matter will be brought before the judge or a jury on the times initially set in the scheduling orders.

Alternate Dispute Resolution in the District Court. The District of Delaware's Alternative Dispute Resolution Program uses magistrate judges to conduct mediation, settlement conferences, binding and nonbinding arbitrations, early neutral evaluations, and summary jury trials on a case-by-case basis. Counsel and the litigants are encouraged by the court to explore alternative dispute resolutions with the magistrate judge assigned to the case. All civil cases, except those filed by prisoners, are eligible for ADR. The ADR options are discussed during the initial Rule 16 scheduling conference, and the district judge may include in the case management order a referral to a magistrate judge for ADR. The parties may also stipulate to ADR.

Referral Method. During the initial Rule 26 scheduling conference, the parties are advised of the availability of ADR through the services of a magistrate judge. During that conference, the district judge will explore with the parties their interest in the ADR process. All district judges have standard provisions in their scheduling orders referring a case for ADR, which usually include contact with a magistrate judge for further discussion regarding ADR.

After referral has been made, the magistrate judge will notify the parties through an order as to the date and time of a teleconference to discuss the form of alternative dispute resolution to be used, the procedures to be followed, including the submission of materials for review prior to the dispute resolution conference, and the timing for that conference. Dispute resolution conferences will not be scheduled prior to the Rule 16 scheduling conference, unless referred or ordered by the district judge. Parties may opt out of participating in the ADR process only with consent of the court.

Timing and Nature of Submissions Required Before the Mediation Session. Usually, each party must provide the magistrate judge with a mediation statement setting forth the party's position concerning the issues to be resolved through mediation not less than 10 days prior to the mediation conference. This mediation statement does not become part of the court record, is not exchanged among the parties or counsel (unless the parties so desire), and is not provided to the trial judge. Page limitations are imposed for the mediation statements.

Contents of the Mediation Statement. The mediation statements may be in memorandum or letter format. Unless otherwise ordered, mediation statements are required to contain the following headings and a discussion of each topic as described below.

- **The Parties.** A description of who the parties are, their relationship, if any, to each other, and by whom each party is represented, including the identity of all individuals who will be participating on behalf of a party during the mediation conference.
- **Factual Background.** A brief factual background clearly indicating which material facts are not in dispute and which material facts remain in dispute.
- **Summary of Applicable Law.** A brief summary of the law, including applicable statutes, cases, and standards. Copies of any unreported decisions (including decisions from this jurisdiction) that counsel believes are particularly relevant should be included as exhibits.

- **Honest Discussion of Strengths and Weaknesses.** An honest discussion of the strengths and weaknesses of the party's claims and/or defenses.
- **Settlement Efforts.** A brief description of prior settlement negotiations and discussions, including the most recent offers or demands exchanged between the parties and the reasons for rejection, and the party's assessment as to why settlement has not been reached.
- **Settlement Proposal.** The party's proposed term(s) for a resolution, identifying any interests or issues not directly involved in the matter that may frustrate or further settlement. If the party has any suggestions as to how the court may be helpful in reaching a resolution, such suggestions should also be described.
- **Fees and Costs.** Separate lists of each of the following: (i) attorneys' fees and costs incurred to date, (ii) other fees and costs incurred to date, (iii) good faith estimate of additional attorneys' fees and costs to be incurred if the matter is not settled, and (iv) good faith estimate of additional fees and costs to be incurred if the matter is not settled.

In addition to addressing the topics listed above, the parties are encouraged to include other information that may assist the resolution process. Crucial or pertinent documents or other similar evidence or a summary of such documents may be submitted with the mediation conference statement.

Trial counsel, counsel who is familiar with the case, and representatives or decision makers of each party with full authority to act on such party's behalf, including the authority to negotiate a resolution of the matter and to respond to developments during the mediation process, must attend the mediation conference. Full authority means that those participants on behalf of a party should be able to make independent decisions and have knowledge or understanding of the dispute and business objectives/operations of their company to generate and consider solutions and be able to address the negotiation dynamics in mediation. Full authority is not just settlement authority. Parties who fail to appear may be subject to a rule to show cause and sanctions.

Duration of the Mediation Process. Generally, a mediation session is scheduled to last approximately eight hours. Trial counsel and the litigants are encouraged to continue the process with or without court assistance after the first session. Depending upon the case, the first session may be sufficient to determine whether the matter can be resolved through mediation. It is not

uncommon, however, for a subsequent session to occur or for the magistrate judge to continue negotiations through telephonic or email discussions.

Mediation Logistics and Location. The magistrate judge, in consultation with counsel and the litigants, establishes the time for mediation. Mediation sessions take place at the courthouse. The magistrate judge determines the length and timing of the sessions and the order in which issues are addressed.

Filing of Mediation Outcome. Generally, the mediation outcome is not made part of the court record. Notification is provided to the referring judge by the magistrate judge as to the outcome of the process. If the first mediation session does not resolve the case, the parties are consulted before the close of that session to determine whether further mediation or other forms of ADR would be appropriate. The date and time of any additional mediation conferences or follow-up teleconferences may be scheduled at that time.

If settlement is reached on all issues during the mediation conference, a written agreement in principle regarding the settlement terms may be drafted, or a record of the agreement may be made through a court reporter. If settlement is reached on some issues, a stipulation of dismissal on those issues should be filed as soon as conveniently possible, which also identifies those issues that remain. The magistrate judge retains jurisdiction over any disputes that may arise in drafting of the final settlement documents.

Confidentiality. Information disclosed to the magistrate judge during mediation, including the contents of any written submissions, is confidential and may not be disclosed to another party without the consent of the disclosing party. Further, such information may not be used in any litigation, absent a court order. Violation of confidentiality may subject the violator to sanctions.

UNITED STATES BANKRUPTCY COURT FOR THE DISTRICT OF DELAWARE

The United States Bankruptcy Court for the District of Delaware sits in Wilmington and has a leading role among U.S. bankruptcy courts in the adjudication of large-scale, complex corporate bankruptcies. Title 28 of the United States Code provides for bankruptcy venue in a corporate debtor's state of incorporation, among other options. As a result of Delaware's preeminence as an incorporation venue, Delaware is thus an available venue option for many corporate debtors. The expertise of the Delaware Bankruptcy Court makes it not only an available, but also a preferred, venue.

Federal Venue Statute. In seeking bankruptcy protection, a company typically has a range of different options to consider in determining where to file its bankruptcy petition. Section 1408(1) of title 28 of the United States Code allows a company to file for bankruptcy in, among other places, the jurisdiction in which it is incorporated or the jurisdiction in which it maintains either its principal place of business or principal assets. Accordingly, any company that is incorporated or domiciled in Delaware may file for bankruptcy in the United States Bankruptcy Court for the District of Delaware. Because Delaware has long been the state of incorporation for a majority of America's largest companies, the Delaware Bankruptcy Court serves as an option for such companies when deciding where to file a bankruptcy petition.

Section 1408(2) of title 28 provides that an entity may commence a bankruptcy case in the district where a case is pending concerning such person's affiliate, general partner, or partnership. This provision is frequently referred to as the "affiliate filing rule" and allows affiliated entities to file their bankruptcy petitions in the same venue even if such entities may be domiciled in different states. For example, following the filing of a bankruptcy petition in Delaware by a Delaware entity, that entity's affiliates may also commence their cases in the Delaware Bankruptcy Court. The term "affiliate" includes (i) any "entity that directly or indirectly owns, controls, or holds with power to vote, 20 percent or more of the outstanding voting securities of the debtor" and (ii) any "corporation 20 percent or more of whose outstanding voting securities are directly or indirectly owned, controlled, or held with power to vote, by the debtor, or by an entity that directly or indirectly owns, controls, or holds with power to vote, 20 percent or more of the outstanding voting securities of the debtor."

Most major companies, if not themselves already Delaware-incorporated, have Delaware-incorporated affiliates and thus have the ability to choose Delaware as a bankruptcy venue capable of providing comprehensive restructuring relief for the entire business group as a whole. The Delaware Bankruptcy Court routinely approves requests from affiliated debtors to have their cases jointly administered for administrative efficiency.

Delaware as a Popular Venue Option. In deciding among possible bankruptcy venues, a corporate debtor will consider, among other factors, the expertise, consistency, convenience, and service of a jurisdiction's courts. The Delaware Bankruptcy Court is popular because it excels in each of these categories.

The Delaware Bankruptcy Court has been a leading bankruptcy venue for large companies for decades due to its manageable docket and pro-reorga-

nization approach favoring the “fresh start” premise adopted by Congress in the Bankruptcy Code. The court has proven to be consistently user-friendly. Omnibus hearing dates in major cases can be scheduled months in advance, and emergency scheduling can be accomplished speedily and easily. The well-organized office of the court’s clerk is responsive and progressive.

The court’s status as one of the country’s busiest and most respected bankruptcy courts resulted in expansion of the bankruptcy bench in 1993 and again in 2005. The court now has six sitting bankruptcy judges. The expanded bench has a reputation for sound rulings and a consistent approach to large and complex chapter 11 cases. The court regularly handles difficult, major restructurings. This experience adds to the judicial expertise of the bench, providing an efficient and expert court.

The court is known for the speed with which chapter 11 debtors are able to reorganize. An extensive academic analysis of bankruptcy venue selection by Kenneth M. Ayotte and David A. Skeel Jr., *Why Do Distressed Companies Choose Delaware? An Empirical Analysis of Venue Choice in Bankruptcy*, concluded that “Delaware is similar to other high-experience courts in terms of the likelihood of reorganization controlling for firm characteristics, but is a standout in terms of speed . . . requir[ing] approximately 40 percent less time to complete than an equivalent case in another court.” This is particularly true when it comes to a debtor’s ability to confirm a “prepackaged” chapter 11 plan (where a plan of reorganization has been fully negotiated and solicited in advance of the bankruptcy petition being filed). Prepackaged bankruptcy cases occur perhaps more frequently in Delaware than any other venue, and typically involve the court conducting a hearing to consider confirmation of a debtor’s chapter 11 plan within 40 days of the debtor’s chapter 11 petition.

The efficiency of the court serves the interests of debtors and creditors alike. Motions seeking to transfer larger cases out of Delaware are rare. Many creditors familiar with corporate bankruptcies, including trade creditors and lending institutions, are as comfortable as prospective debtors with a Delaware venue. Major lending institutions routinely recommend Delaware to struggling companies as an appropriate bankruptcy forum.

Applicable Local Court Rules. The Delaware Bankruptcy Court has adopted Local Rules of Bankruptcy Practice and Procedure. The Local Rules apply to practice before the court to the extent they are not inconsistent with the Bankruptcy Code and the Federal Rules of Bankruptcy Procedure. The Local Rules are amended from time to time by the court’s chief judge, subject to the approv-

al of the chief judge of the Delaware District Court. The application of the Local Rules in any case or proceeding may be modified by the Delaware Bankruptcy Court in the interest of justice. The court's judges routinely take into account issues of fairness and prejudice when ruling on requests for waiver of modification of the Local Rules. The current version of the Local Rules supersedes all previous Local Rules, but does not affect any general order issued by the court or any chambers procedures of any of the court's judges.

The Delaware District Court has also promulgated Local Rules of Civil Practice and Procedure. These Delaware District Court Local Rules need to be adhered to in certain instances during a case pending in the Delaware Bankruptcy Court, including, for instance, briefing in connection with a motion to withdraw the reference from the Delaware Bankruptcy Court, and appeals of Delaware Bankruptcy Court orders or rulings made to the Delaware District Court. Beyond the need to reference the Delaware District Court Local Rules, practitioners in the Delaware Bankruptcy Court may also need to become familiar with the General Chambers Procedures of the Delaware Bankruptcy Court, as well as the individual judge's chambers procedures.

CHAPTER NINE

FINANCIAL SERVICES

Innovative and flexible banking and financial services laws have established Delaware as a national financial center.

Delaware is an established national financial center. Despite Delaware's small size, there are more than 75 state or federally chartered financial institutions in Delaware offering a wide range of financial services to commercial and retail customers, both in Delaware and across the world. Many of these financial institutions offer active commercial loan and other credit programs. Delaware is home to many of the largest credit card issuers in the United States, such as Bank of America, J.P. Morgan Chase, Discover Bank, and Barclays Bank Delaware.

Entry into the Delaware banking market under Delaware law may be accomplished through the de novo formation of a banking entity or the establishment of a de novo branch, by acquisition of an entire bank, or by an interstate merger transaction (which includes a merger, a consolidation, or an asset purchase involving an out-of-state bank and a bank located in Delaware). Delaware generally permits, with the prior approval of the Delaware Bank Commissioner, out-of-state bank holding companies or their subsidiaries to acquire or retain ownership or control of banks located in Delaware. Only existing Delaware banks may engage in an interstate merger transaction with an out-of-state bank if the resulting bank from such transaction will be an out-of-state bank. An existing Delaware bank is a Delaware state or national bank the initial Delaware charter or authorization of which to conduct a banking business in Delaware bears an effective date not less than five years prior to the effective date of the interstate merger transaction. Any branches of a disappearing Delaware bank in an approved interstate merger transaction resulting in an out-of-state bank may be retained by the resulting out-of-state bank as interstate branches.

ADVANTAGES OF DELAWARE FINANCIAL INSTITUTIONS

Financial Center Development Act. Delaware is an established financial center due in great part to the enactment of legislation that modernized its banking laws in order to create a banking code that recognizes both commercial practices and the future needs of providers of commercial and consumer credit in a changing environment. The Financial Center Development Act (the FCDA), enacted in 1981 and expanded in 1984, permitted the acquisition of newly established Delaware state-chartered or national banks located in Delaware by an out-of-state bank holding company or its subsidiary so long as certain specified conditions were satisfied, which conditions could be waived by the Bank Commissioner. Many local banks were formed under this legislation.

Usury and Exportation of Interest Rates. Since the passage of the FCDA, Delaware banks have not been subject to usury limitations under Delaware law in extending credit to customers. The combination of Delaware law and federal law enables Delaware banks to export interest rates across state lines free of the usury limitations imposed by other states. For this reason, many commercial and consumer banks choose Delaware as the location from which they conduct a nationwide banking business.

Regressive Tax Rate Structures. Banking organizations in Delaware enjoy low, regressive tax rate structures that decrease as taxable income or assets increase. Banking organizations may choose one of two regressive tax rate structures, each of which has relative advantages based on the nature and level of the specific banking business. Employment tax credits may also be available to banking organizations that increase the number of qualified employees in Delaware. (See Chapter Four, “**Taxation – Corporate Income Tax – Banking Organizations.**”)

Innovation in Permissible Activities. Delaware is a proven leader in innovation within the financial services industry. Delaware was among the first states to permit banks to engage in securities and insurance underwriting activities. Delaware state-chartered banks are also granted other broad activity powers under state law. In some circumstances, enumerated powers granted to Delaware state-chartered banks under the Delaware Banking Code are broader than those granted to national banks under the National Bank Act. Of course, because the deposits of Delaware state-chartered banks are insured by the Federal Deposit Insurance Corporation, reference to federal law restrictions is necessary before acting under any powers granted by Delaware law. Delaware state-chartered banks formed by act of the Delaware General Assembly prior to the enactment of the state corporation law for banks and trust companies may enjoy even broader powers than those enumerated in the Delaware Banking Code.

Advantageous Trust Laws. Delaware is known as a very favorable jurisdiction for the operation of the trust department of a bank, a trust company, or a limited purpose trust bank. Trust companies chartered under Delaware law can be formed either as corporations or limited liability companies. Delaware banks and trust companies are able to offer personal and statutory trust products that offer significant advantages to clients compared to the laws of other jurisdictions. (See Chapter Two, “**Business Entities – Statutory Trusts,**” and Chapter Eleven, “**Personal Wealth Management.**”)

TYPES OF DELAWARE FINANCIAL INSTITUTIONS

State-Chartered Banks and Trust Companies. In 1933, the Delaware Banking Code was established to provide a statutory framework for forming state-chartered banks and trust companies with general banking powers, and if desired, trust company powers. Delaware state-chartered banks and trust companies are granted broad powers under the Delaware Banking Code.

Limited Purpose Trust Companies. In 1982, Delaware enacted legislation permitting the formation of limited purpose trust companies that do not have general banking powers. The legislation was intended to resolve an ambiguity in the Delaware Banking Code as to whether trust company powers may be granted without general banking powers. As of January 31, 2011, there were 18 state-chartered, limited purpose trust companies in Delaware. Some Delaware limited purpose trust companies have been formed by high net worth individuals or families to operate as private trust companies for self-management and administration of trusts, while others have been formed by providers of personal trust services to offer the benefits of Delaware trusts to their clients worldwide. Still others have been formed by major banking organizations to offer corporate trust services. Delaware limited purpose trust companies enjoy all the powers of banks and trust companies under Delaware law, with the exception of accepting deposits or making loans to nonaffiliates. Limited purpose trust companies are not considered banks under the federal Bank Holding Company Act of 1956, as amended.

Nondeposit Trust Companies. Prior to the enactment of the Delaware Banking Code in 1933, a corporation could be incorporated under the General Corporation Law of the State of Delaware with trust company powers granted to it in its certificate of incorporation. Such a corporation may transact a trust company business if it receives a certificate from the Bank Commissioner authorizing it to transact a trust company business. As of January 31, 2011, there were 12 state-chartered nondeposit trust companies authorized to transact a trust company business by the Bank Commissioner. Nondeposit trust companies are not considered banks under the federal Bank Holding Company Act of 1956, as amended.

Credit Card Institutions. Delaware state-chartered credit card institutions that have limited powers may be formed under Delaware law. In particular, a credit card institution may (i) only engage in credit card operations, (ii) not accept demand deposits or deposits that a depositor may withdraw by check or

similar means for payment to third parties or others, (iii) not accept any savings or time deposits of less than \$100,000, (iv) maintain only one office that accepts deposits, and (v) not engage in the business of making commercial loans. In addition, a credit card institution may not be a bank as defined in the federal Bank Holding Company Act of 1956, as amended. A credit card institution may convert to a bank upon application to and approval by the Bank Commissioner. Notwithstanding the statutory authority to establish limited purpose credit card institutions, it is more typical to form a Delaware bank capable of exercising full banking powers and limit the bank's permissible activities in its charter to qualify it for an exception from the definition of a bank under the federal Bank Holding Company Act of 1956, as amended.

State Savings Banks. In 1997, as part of the Banking Industry and Financial Services Act of 1997, Delaware instituted a separate chartering framework for the formation of state-chartered savings banks. Delaware state-chartered savings banks have powers similar to those of Delaware state-chartered banks and trust companies, but must comply with the qualified thrift lender test and restrictions on amounts of commercial loans.

Foreign Bank Branches, Limited Purpose Branches, and Agencies. In 1986, Delaware enacted the Foreign Banking Development Act, which allows a foreign bank to establish and maintain a foreign bank branch, a foreign bank limited purpose branch, or a foreign bank agency and to conduct certain types of banking business in Delaware. Once a foreign bank has obtained a certificate of authority, it may establish and maintain a foreign bank branch, a foreign bank limited purpose branch, or foreign bank agency in Delaware, and engage in a general banking business.

A foreign bank agency may not accept deposits from citizens or residents of the United States or act as a fiduciary. A foreign bank agency may, however, maintain for the account of others credit balances incidental to or arising out of the exercise of its lawful powers. In addition, the Bank Commissioner has the authority to adopt regulations that, notwithstanding the statutory limitations on a foreign bank agency's general banking powers, would authorize a foreign bank agency to accept any deposit or exercise any other power that it could if it were operating in Delaware as a federal agency pursuant to the federal International Banking Act of 1978. The Bank Commissioner has adopted such a regulation. A foreign bank limited purpose branch may, in any event, accept deposits that would be permissible for a corporation organized under Section 25A of the Federal Reserve Act.

A foreign bank may operate a representative office in Delaware, so long as the representative office obtains a license from the Bank Commissioner, engages in representational functions on behalf of the foreign bank, and does not conduct a banking business. To obtain such a license, the foreign bank must submit an application to the Bank Commissioner. The Bank Commissioner will issue a license to the foreign bank to establish and maintain a representative office in Delaware if the Bank Commissioner determines, among other things, that the foreign bank and the management proposed for its Delaware representative office are each of good character and sound financial standing, and the management of both the foreign bank and its representative office is adequate.

Other Types of Delaware Financial Institutions. Delaware's Banking Code permits financial businesses to obtain licenses to conduct specific financial activities in Delaware (and to establish locations outside of Delaware) other than through the bank or trust company chartering process, including, with respect to general consumer lending activities (which may be conducted by Delaware licensed lenders without general usury limitations under Delaware law), acting as a mortgage loan broker; the sale and cashing of checks, drafts, and money orders; the transmission of money; financing the sale of motor vehicles; and the transportation of money and other valuables.

STRUCTURED FINANCE AND SECURITIZATION TRANSACTIONS

Delaware is a leading jurisdiction for structured finance and securitization transactions. There are several statutory advantages in Delaware that have led to its preeminence in these areas. The Delaware Limited Liability Company Act, the Delaware Statutory Trust Act, and the Delaware Revised Uniform Limited Partnership Act provide for the formation of legal entities that permit contractual flexibility. As a result, practitioners can tailor Delaware limited liability company agreements, statutory trust agreements, and limited partnership agreements to provide for bankruptcy-remote entities that are favorably received by rating agencies and investors.

In connection with many securitization transactions, receivables such as mortgage debts, leases, loans, or credit card balances are sold by originators to Delaware bankruptcy-remote entities, which in turn issue securities backed by such assets. Delaware has a unique statute that is intended to facilitate such transactions, the Asset-Backed Securities Facilitation Act. Under this Act, to the extent set forth in the transaction documents relating to a securitization,

any property, assets, or rights purported to be transferred, in whole or in part, in the securitization transaction are deemed to no longer be the property, assets, or rights of the transferor. This Act assists practitioners in structuring transactions as “true sales” under Delaware law.

In order to provide more clarity and confirm existing law and practice in the context of Delaware’s securitization industry, Article 9 of the Delaware Uniform Commercial Code was amended to add an additional safe harbor for identifying certain types of collateral typically involved in securitization transactions. Under that safe harbor provision, a financing statement sufficiently indicates the collateral that it covers if the collateral is accounts, chattel paper, instruments, or general intangibles and: (i) the financing statement provides a description of one or more records in the possession or control of the secured party that identify the specific collateral; (ii) the financing statement indicates that the items described on the record or records in the possession or control of the secured party are accounts, chattel paper, instruments, or general intangibles, or otherwise indicates the nature of the items on the record or records by general description or category; and (iii) the record or records contain confidential information (such as credit card numbers) or a description of 100 or more specific accounts, chattel paper, instruments, or general intangibles. This safe harbor simplifies the preparation of financing statements in connection with certain securitization transactions.

INSURANCE AND CAPTIVE INSURERS

Transacting insurance business in Delaware, as elsewhere, is significantly regulated. The principal regulation of insurance companies in the United States is left to the states. This deference to state regulation of insurance companies is guaranteed by the federal McCarran Act. States generally have adopted a comprehensive, detailed framework for the regulation of all aspects of transacting insurance.

The Delaware Insurance Code provides the statutory framework governing the transacting of insurance in Delaware. In each state, including Delaware, the principal goal in the regulation of insurance companies chartered (in insurance parlance, “domiciled”) in that state is to ensure their financial health and soundness in order to protect policyholders wherever they might be located. Therefore, the fundamental financial health and soundness of insurance companies domiciled in Delaware but selling insurance elsewhere is principally a matter for Delaware. On the other hand,

regulation of the financial health and soundness of insurance companies domiciled in other states but selling insurance in Delaware is principally a matter for the states of domicile of such insurance companies.

In addition to states having the principal regulatory responsibility for insurance companies domiciled in their own state, most states, including Delaware, provide additional regulations for the transacting of insurance business within each of the respective states, even though the principal regulation of the financial health and soundness of such insurance companies might be elsewhere. For example, insurance companies domiciled in other states, before transacting insurance in Delaware, must receive a certificate of authority from the State. There are certain exceptions to this certificate of authority requirement, including the investigation of claims, transactions under a particular insurance policy subsequent to the issuance of the policy governing only subjects of insurance not resident or located within the State of Delaware, surplus lines coverage, reinsurance, and underwriting membership in a regulated insurance exchange. None of these activities occurring in Delaware requires a certificate of authority. In addition, before an insurance company, wherever domiciled, may sell insurance in Delaware, the insurance company must normally file with the Delaware Insurance Commissioner a copy of the form of each policy to be executed and delivered in the State.

All insurers domiciled in Delaware or domiciled elsewhere and transacting insurance business in Delaware must meet certain capital funds requirements as provided in the Delaware Insurance Code. They also must pay certain taxes (generally based upon the amount of premiums collected for policies sold in Delaware) and keep on file with the Delaware Insurance Commissioner copies of their financial statements and any examinations made upon them by the insurance commissioners of other states. The basic insurance tax in Delaware is 1.75 percent on net premiums on policies written in the State. There are certain exceptions and graduated taxes, particularly for employer-owned insurance policies. Insurers issuing workers' compensation policies or employer liability risks in the State pay a different tax. Insurance companies domiciled in Delaware that do not write 50 percent of the total premium on property or persons residing in Delaware and that have minimal employees in the State are assessed an annual privilege tax that ranges between \$10,000 and \$95,000 per year, depending upon the size of the insurance company.

Chapter 69 of the Delaware Insurance Code expressly permits various forms of captive insurance companies. Captive insurance companies have gained favor throughout the world in recent years as an alternative method of managing risks. Delaware is an attractive domicile in which to form a captive insurance company, as Chapter 69 was recently rewritten to address current market trends and needs. As such, the Delaware Insurance Code expressly permits pure captives, association captives, agency captives, sponsored captives, industrial insured captives, special purpose captives, special purpose financial captives, and risk retention groups, whether domestic, foreign, or alien, and branch captives. In most cases, the captive insurance company may be a stock corporation, nonstock corporation, limited liability company, partnership, limited partnership, or statutory trust. Captive insurance companies can provide administrative efficiencies, greater management and control, and flexibility of investment policies in connection with meeting the insurance requirements of the insured. A major advantage that Delaware provides is a simple premium tax structure that imposes a 0.2 percent tax on direct premiums capped at \$125,000 annually and a 0.1 percent tax on assumed reinsurance premiums capped at \$75,000 annually. Generally, captive insurance companies have far greater investment flexibility than their traditional counterparts, as in most circumstances a captive insurance company need not comply with any restrictions on allowable investments as set forth in the Delaware Insurance Code.

In Delaware, the Insurance Commissioner is the chief officer of the State charged with the regulation of insurance activities. The Insurance Commissioner is elected to a four-year term at the general election. The Insurance Commissioner is also the head of the Delaware Department of Insurance and has broad, general powers to enforce and execute the duties imposed by the Delaware Insurance Code. The powers of the Insurance Commissioner include the power to make reasonable rules and regulations with respect to insurance companies, to issue orders with respect to their operations, to enforce lawful orders through the attorney general of the State, to conduct investigations and examinations of insurers, and to regulate Delaware insurance agents generally.

The Delaware Insurance Code also gives to the Insurance Commissioner broad powers to seize control of a Delaware insurer when the Insurance Commissioner believes that such insurer is impaired or potentially insolvent, and powers to rehabilitate or, under certain circumstances, liquidate such insurer. Delaware insurance companies subject to rehabilitation or liquidation orders generally have a right to a hearing before the Insurance Commissioner

and also the right to appeal an order of the Insurance Commissioner to the Delaware Superior Court. The liquidation of insurance companies domiciled in Delaware is subject to the Uniform Insurers Liquidation Act, a part of the overall Delaware Insurance Code. The Delaware Uniform Insurers Liquidation Act is similar to liquidation acts in other states.

The Department of Insurance is organized into several sections, as follows:

Bureau of Captive and Financial Insurance Products.

- Regulates captive insurance companies consistent with their nature and purpose.
- Provides flexibility and opportunity to captive insurance companies and to persons utilizing them.
- Fosters economic development in Delaware through the growth of the captive insurance industry.

Bureau of Company Examination, Regulation and Guaranty. To ensure reliable insurance coverage at reasonable rates for Delaware consumers, this bureau:

- Reviews applications to do business in Delaware.
- Monitors the financial operations of the 1,500 foreign and 150 domestic insurers currently licensed in Delaware.
- Monitors the market conduct of insurers operating in Delaware.
- Approves or contests insurers' rate filings.
- Rehabilitates or liquidates financially impaired insurers.

Consumer Services and Investigations Division. To protect the welfare of insurance consumers, this division:

- Provides information on how to make decisions that can lower the cost of insurance and increase the value consumers receive.
- Assists consumers in resolving conflicts with insurance companies, health coverage providers, and agents.
- Provides arbitration hearings as a low-cost alternative to civil litigation to resolve disputed consumer claims.
- Investigates concerns regarding all types of insurance and utilizes consumer input to review market trends and statute and rule violations, and to develop changes to the insurance law.

Producer Licensing and Continuing Education Division. To ensure competency and ethical conduct by insurance agents, brokers, limited agents, adjusters, appraisers, and consultants, this division:

- Develops and administers tests for entry into the field.
- Maintains permanent records on the current 33,000 insurance professionals.
- Administers the continuing education program.
- Provides consumers information about the licensing status of a producer.

Fraud Prevention Bureau. To reduce the cost of insurance fraud to consumers, this bureau:

- Investigates property and casualty, auto, life, health, workers' compensation, provider, and agent insurance fraud.
- Provides a focal point for the anti-fraud efforts of insurance company investigators, law enforcement agencies, and prosecutors to achieve a cooperative and coordinated approach to the detection, investigation, and prosecution of insurance fraud.

STATE BLUE SKY AND OTHER SECURITIES ISSUES

For the commercial enterprise seeking to raise the financing necessary to start, continue, or expand its business, federal and state securities law compliance is an important matter to consider. Delaware is one of the approximately 37 states that enacted a state securities statute patterned after the 1956 Uniform Securities Act. However, the Delaware Securities Act, enacted in 1973 and amended several times since, contains many variations from the Uniform Securities Act.

Under the Delaware Securities Act, no security may be offered or sold in the State unless registered under such Act or an exemption from registration applies. The Delaware Securities Act makes it unlawful for a person to commit fraud in the offer, sale, or purchase of a security. The Delaware Securities Act also regulates the activities of broker-dealers, investment advisers, and agents that transact business in the State.

Offer or Sale of Securities in Delaware. To determine whether the Delaware Securities Act would apply to proposed fund-raising activities, one must consider whether an offer or sale of a security would occur in Delaware. The Delaware Securities Act defines "security" broadly to include, without limitation, any note, stock, treasury stock, bond, debenture, evi-

dence of indebtedness, or investment contract. This definition is similar to that used in the federal Securities Act of 1933, as amended.

Two very common approaches to raising financing are the issuance by an entity of its equity or debt instruments. These instruments are generally included in the Delaware Securities Act's definition of security.

Exemptions from Registration. Certain types of securities are exempt from registration under the Delaware Securities Act. For the commercial enterprise, its securities would be exempt from registration if, among other things, (i) the enterprise is in one of certain specified businesses and is subject to the jurisdiction of the Interstate Commerce Commission or is a registered holding company under the federal Public Utility Holding Company Act of 1935; (ii) such securities are listed on certain exchanges, including, without limitation, the New York and the American Stock Exchanges; (iii) the enterprise is a nonprofit religious organization meeting certain specified financial and other conditions; (iv) such securities constitute short-term commercial paper meeting certain specified requirements; or (v) such securities are traded pursuant to the National Association of Securities Dealers Automated Quotations National Market System.

Certain types of transactions are also exempt from registration under the Delaware Securities Act. In order for some of the transactional exemptions to apply, a prescribed notice must be filed with, and a fee must be paid to, the office of the Delaware Securities Commissioner. These transactional exemptions include, among other things, (i) offers and sales in compliance with Rule 505 or 506 of federal Regulation D, (ii) offers to sell to existing security holders if certain specified conditions are met, (iii) limited offerings, (iv) offers and sales to institutional investors, and (v) offers and sales to accredited investors.

For the commercial enterprise, one of the more important exemptions to registration exists for transactions exempt from registration under the federal Securities Act of 1933 under Rule 505 or 506 of Regulation D promulgated thereunder (including the sale of federal covered securities in a private offering under Rule 506). The enterprise issuing and selling the securities must file with the Delaware Securities Commissioner a copy of federal Form D and Form U-2, Uniform Consent to Service of Process, within 15 days after the first sale of a security in Delaware.

Another important exemption is the limited-offering exemption. This exemption applies only if offers are directed to not more than 25 purchasers in Delaware (although certain persons are not included in calculating the number

of purchasers) during any 12-month period. In all sales to nonaccredited investors, the enterprise must have a reasonable basis to believe that (i) each offeree has the financial experience and knowledge to evaluate the securities, or (ii) the investment is suitable for each offeree based upon the facts, if any, disclosed by the offerees as to their other security holdings, financial situation, and needs. No commission, fee, or other remuneration can be paid or given to anyone for soliciting prospective purchasers in Delaware unless the person is properly registered. The enterprise must file with the Delaware Securities Commissioner federal Form D (if the form is being filed by the enterprise with the U.S. Securities and Exchange Commission (the SEC)) or Delaware Form D-1 not later than 15 days after the first sale of securities in Delaware or within six months after the commencement of the offering, whichever occurs first.

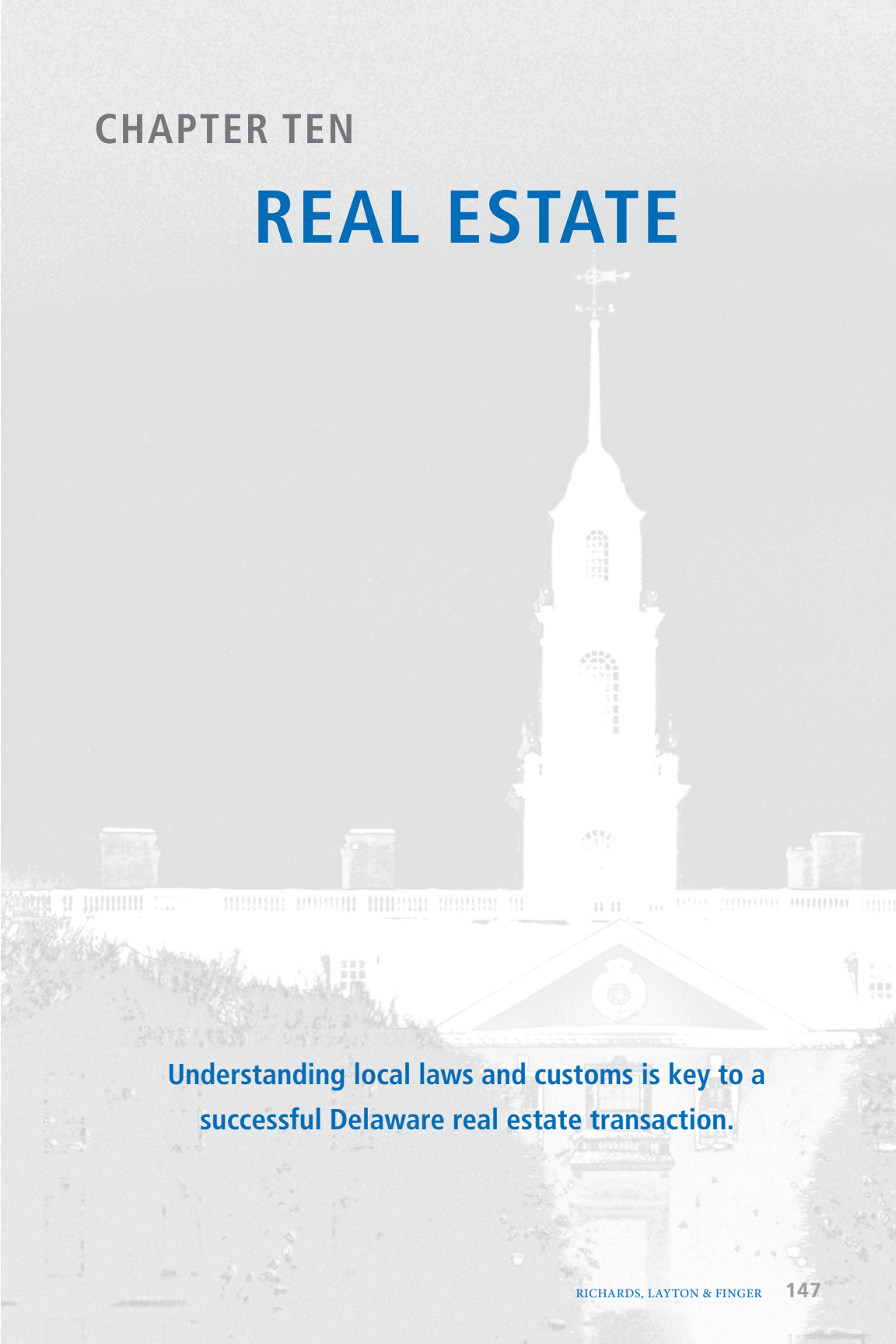
Any offer or sale by the enterprise to an institutional buyer will be exempt from registration, notice, and sales literature filing requirements. Institutional buyers include accredited investors (as defined in Rule 501 of Regulation D), qualified institutional buyers (as defined in SEC Rule 144A), and corporations, partnerships, trusts, estates, or other entities having a net worth of at least \$5 million.

Registration. An offering of securities may be registered in Delaware by coordination or by qualification. Registration by coordination is available for securities being registered with the SEC and involves the filing with the Delaware Securities Commissioner of a copy of the registration statement filed with the SEC and certain other forms and the payment of a fee. The registration becomes effective once the federal registration statement is effective, all required documents and information have been filed with the Delaware Securities Commissioner, the Delaware registration statement has been on file for 10 days, and a statement about offering prices and underwriting discounts and commissions has been on file with the Delaware Securities Commissioner for at least two business days, unless a stop order is in effect or proceedings for such an order are pending.

Registration by qualification is available for any security and involves the filing with the Delaware Securities Commissioner of a registration statement containing certain prescribed information and certain other forms and the payment of a fee. Registration is effective upon order of the Delaware Securities Commissioner.

CHAPTER TEN

REAL ESTATE



Understanding local laws and customs is key to a successful Delaware real estate transaction.

PURCHASE AND SALE OF REAL ESTATE

The laws and customs governing the purchase and sale of real estate in Delaware do not differ greatly from those of most other states. Although Delaware has some peculiarities in this regard, more often those peculiarities vary from county to county or between municipalities within the State. Understanding the laws or customs in a particular locality can be more important to the success of a real estate transaction than state laws.

ROLE OF BROKERS AND CONSULTANTS

Because local custom is so important, professional consultants (such as attorneys, brokers, and planners) generally provide a valuable service in these transactions. A company new to Delaware will usually contact a real estate broker for the purchase or leasing of property. Generally, the broker remains the agent of the seller as a matter of Delaware law, even though a broker may be retained by the purchaser to locate and help negotiate for possible properties. On the other hand, where the broker is the purchaser's agent, the broker is responsible for making certain disclosures regarding the broker's role as agent for the purchaser. Brokers can also serve in a dual agency relationship with the seller and purchaser.

TYPICAL CONTRACT TERMS

The negotiation of sales contracts or options can follow many paths and take many forms. Delaware has been moving towards statewide, standardized form contract documents for residential real estate transactions. In 2007, the Delaware Association of Realtors introduced an industry-standard contract for residential sales. This form is widely utilized as the contract form for the purchase and sale of residential property statewide. In 2009, the General Assembly enacted the Delaware Uniform Common Interest Ownership Act (DUCIOA), largely a consumer-protection statute that provides for seller disclosures of certain facts about residential common interest properties. DUCIOA does not prescribe any particular forms for these mandatory disclosures, but it does require such disclosures to contain specific information. Standard forms will likely emerge within the residential real estate community addressing DUCIOA's mandatory reporting requirements. DUCIOA does not apply to any nonresidential common interest community, unless the community's governing documents elect to have it apply.

No standardized forms of contracts or options are used throughout the State for commercial real estate transactions; however, most commercial contracts or

options routinely contain certain types of provisions. For example, most contracts allow a purchaser a period of time within which to examine the physical condition and other aspects of the property and within which to arrange the financing necessary to purchase the property. During this period, the purchaser might examine the title to the property, have a structural engineer inspect the property, or perform an environmental audit of the property for compliance with environmental laws. During this period of examination and inspection, the purchaser is often not at risk for the purchase price, and, if the examination or inspection discloses an unacceptable condition, the purchaser may have the right to terminate the contract.

There are also some customary allocations of risks and costs that are generally found throughout the State. For example, the purchaser will usually obtain its own examination of title insurance, at its cost. The purchaser will usually prepare the transfer documents at its cost and pay for recording the transfer documents in the land records.

Delaware law requires that contracts for the sale of undeveloped land or that provide for seller financing contain certain terms and conditions specified by statute. Delaware law also provides certain limitations in connection with conditional sales agreements involving residential real estate, regulating the period of time that such contracts are capable of remaining unperformed.

TITLE INSURANCE

Delaware is characterized as an attorney-agency state for title insurance. In other words, title insurance is obtained from and written by attorneys in private practice who are acting as agents for one or more title insurance companies. Delaware is also a filed-rate state in that the rates for title insurance filed with the State by an insurance company are not subject to further negotiation by the insurance company. Not all title insurance companies have filed the full range of ALTA endorsements, and some endorsements typically available in other states are not routinely available in Delaware.

TRANSFER TAXES

Most transfers of real property in Delaware are subject to realty transfer tax. Transfer tax is payable at the time the transfer document (usually a deed) is recorded in the appropriate recording office. The State and many of the other political subdivisions imposing a realty transfer tax have their own reporting forms that are filed with the transfer document at the time of recording and payment of the transfer tax.

In most jurisdictions within Delaware, the transfer-tax liability is divided equally between the purchaser and the seller in the absence of any agreement by the parties to the contrary. (See Chapter Four, “**Taxation – Sales and Use Taxes – Realty Transfer Tax.**”)

REGISTRATION AND REGULATION

Aside from federal requirements, such as the Foreign Investment in Real Property Tax Act of 1980, as amended, there are few regulations of purchases and sales imposed at the state or local level. Although there may be requirements for the registration of a foreign corporation, foreign limited partnership, or other entity under other applicable laws governing those entities (including the need for certain foreign entities to register if they are to own real property in Delaware), and although the tax laws may impose certain obligations, no state law obligates foreign entities that are purchasing or selling real estate to register that purchase or sale with any state or local agency. Other state laws should be reviewed, however, in order to determine the requirements with respect to registration of various entities. Those might include the qualification of a foreign corporation to do business in the State or the filing of a “fictitious name” certificate for an entity in the Office of the Prothonotary of the county in which such entity will be owning and operating real estate. Generally, state environmental laws do not require registration or notice as part of real estate transfers, other than requirements that may apply to the transfer or change of ownership of facilities or equipment that are subject to operational permits. In 2008, the General Assembly enacted a statute governing the transfer or closure of a chemical or hazardous substance establishment that will impose requirements on the transferor and transferee of such an establishment. This statute is not effective until the applicable agency promulgates regulations, which has not occurred as of the date of this publication.

LAND USE AND DEVELOPMENT

Each of the three Delaware counties and most of the incorporated municipalities throughout the State have separate and often very different zoning, subdivision, and land development regulations. The differences relate not only to different types of zoning classifications, but also to different procedures for rezonings; different types of development plan requirements, formats, and procedures; and different scopes of those various regulations. Delaware has virtually no statewide land use regulation other than environmental and environmental-related regulation (*e.g.*, Underground Storage Tank Act, Coastal Zone Act, wetlands regulations, storm water management controls, etc.). The

process of rezoning or obtaining subdivision or land development plan approvals is, therefore, primarily a localized one.

The diverse state of zoning and other land use regulation throughout Delaware does not usually result in insurmountable difficulties in obtaining rezonings or other land use approvals. It does mean, however, that the process must be approached carefully and with knowledge of the particular regulations and practices of the jurisdiction in which the property is located.

The decentralization of much of the land use regulation in Delaware may result in convenience for the property owner or developer. Depending upon the locality, most permits and approvals will be generated by, or at least coordinated through, a single office for an entire real estate development project. A state land use planning law allows for a streamlined approval process from state agencies. All of this can mean ease, efficiency, and cost-effectiveness.

LEASING

All forms of real estate leasing are common in Delaware, including land or ground leases. Delaware's Residential Landlord-Tenant Code applies to most, but not all, residential real estate rental agreements. Short-term beach rentals, for example, are not covered by the residential code. A Commercial Landlord-Tenant Code applies to most commercial real estate rental agreements. For purposes of the commercial code, rental agreements generally include all commercial and industrial leases, but not land or ground leases. The scope of this code is very limited, and it imposes few practical constraints on the parties' freedom to contract as they wish. Farm and manufactured home community leases are each governed by a separate statute.

There is no form of lease in general use throughout the State, although there are industry-created forms in general circulation. Leases are based on the form of lease employed by an individual landlord or negotiated by the parties.

A faint, grayscale background image of the Delaware State Capitol building, featuring a prominent central clock tower and a pedimented roof with a crest.

CHAPTER ELEVEN

PERSONAL WEALTH MANAGEMENT

Delaware's favorable trust laws, preeminent judicial system, flexible investment rules, and tax advantages make Delaware a center for personal wealth management.

Delaware long ago developed a body of trust and tax law that has led people from throughout the United States and abroad to establish trusts in the State. Several of the provisions discussed below are not unique to Delaware, but the existing body of state law coupled with Delaware's continual process to maintain a favorable trust climate continue to make it the best place to have personal trusts. For example, Delaware is an attractive location for many trusts because, unlike most other states, Delaware does not impose an income tax on, or require the filing of a return to report, non-Delaware source ordinary income accumulated in or capital gains incurred by an irrevocable resident trust, provided that no remainder beneficiary lives in the State. Accordingly, an irrevocable trust without a Delaware remainder beneficiary will not be subject to any Delaware income tax because all income will either be distributed (which will result in a distributions deduction) or will be accumulated (which will result in a deduction for Delaware purposes). Similarly, trusts are frequently located in Delaware in order to minimize court costs and to preserve confidentiality. Trust administration ordinarily is not supervised by the Delaware courts, and this practice can produce substantial savings in accounting and other court costs over the duration of a trust. However, if judicial involvement is required (for example, when the proper interpretation of the governing instrument is uncertain or a fiduciary is believed to be acting in breach of a duty), prompt and efficient relief is available in the Delaware Court of Chancery.

PERPETUAL TRUSTS

In 1995, Delaware enacted legislation that permits stocks, bonds, and other personal property to remain in trust forever. Real property held in trust continues to be governed by a 110-year limitation, enacted in 1986, when the common law rule against perpetuities for real and personal property was repealed in Delaware. This limitation can be avoided, however, by placing real property in a limited liability company or family limited partnership and then placing the LLC or partnership interests in trust. Interests in those types of entities are personal property under Delaware law and thus not subject to the 110-year limitation. Accordingly, unlike many other states, Delaware permits the creation of a perpetual trust for other than charitable or similar purposes. An individual thinking about creating a trust to attempt to obtain the benefit of the GST exemption from the federal generation-skipping transfer tax for as long as legally possible should consider Delaware.

DIRECTION TRUSTS

Delaware has an established practice of permitting someone other than the trustee to make investment decisions for particular assets (e.g., closely held stock) or with the hope of maximizing the trust's investment performance. Delaware law facilitates the use of investment advisers by making it clear that a trustee may follow the direction of an adviser authorized by the governing instrument to give such direction without breaching the trustee's fiduciary responsibility and that the trustee will be liable for doing so only in cases of willful misconduct. To recognize this diminished responsibility, Delaware corporate trustees customarily charge lower fees to administer direction trusts than trusts over which they have investment responsibilities.

Even if a trust does not provide for the appointment of a direction investment adviser, a trustee may hire an agent to advise it concerning trust investments. Because the trustee is responsible for the agent's performance, however, Delaware corporate trustees do not charge less to administer trusts for which they have hired agents.

EFFECTIVE ASSET PROTECTION

Delaware long has enforced spendthrift trusts. Under Delaware's recently revised statute, a creditor of a beneficiary of such a trust has only such rights to the trust property as are afforded the creditor by the terms of the instrument, and no limit is placed on the amount that may be sheltered from creditors' claims. Although the courts have created an exception for obligations to support a spouse, Delaware law provides virtually complete protection from the claims of creditors of a beneficiary other than the settlor. Unlike the law in some other states, Delaware law bars a creditor from seizing the interest of a beneficiary even when the beneficiary commits a willful tort.

ASSET PROTECTION TRUSTS

Under Delaware's Qualified Dispositions in Trust Act, a person may create an irrevocable Delaware trust (i) that should not be reachable by creditors, and (ii) from which he or she still may benefit. Such a trust may also be structured to be a completed gift for federal gift-tax purposes and to be excludable from the settlor's gross estate for federal estate-tax purposes.

To take advantage of the Delaware Qualified Dispositions in Trust Act, the settlor must make a qualified disposition, which is a disposition by a settlor to a qualified trustee or qualified trustees by means of a trust instrument. The

qualified trustee must be an individual (other than the settlor) who resides in Delaware or any entity authorized by the law of Delaware to act as a trustee and whose activities are subject to supervision by certain regulatory authorities. Provided that there is at least one Delaware qualified trustee, it is possible to appoint individual co-trustees who do not reside in Delaware or non-Delaware corporate co-trustees. The qualified trustee or qualified trustees must maintain or arrange for custody in Delaware of some of the trust property, maintain records for the trust, prepare or arrange for the preparation of fiduciary income tax returns, or otherwise materially participate in the administration of the trust. The trust instrument must provide that Delaware law governs the validity, construction, and administration of the trust, specify that the trust is irrevocable, and contain a spendthrift clause. The terms of the trust may permit the settlor to retain (i) a special testamentary power of appointment, (ii) the power to act as investment advisor, (iii) the power to veto distributions, (iv) the right to receive current income distributions, (v) the right to receive annual payments of up to 5 percent of the principal of the trust, (vi) the right to receive payments from a charitable remainder unitrust or annuity trust, (vii) the right to receive principal distributions under an ascertainable standard, (viii) the right to use real property held in a qualified personal residence trust, or (ix) the right to receive discretionary distributions of income or principal to pay income taxes due on the trust.

The Delaware Qualified Dispositions in Trust Act bars original actions and actions to enforce judgments, including judgments entered elsewhere, and it requires any action involving a Delaware asset protection trust to be brought in the Delaware Court of Chancery. Any action to set aside a qualified disposition must be based on the Delaware Uniform Fraudulent Transfers Act, subject to limited exceptions related to child support, property divisions, and alimony or certain tort liabilities incurred before the date of the disposition. If a creditor's claim under the Delaware Uniform Fraudulent Transfers Act arose before the qualified disposition was made, the creditor must bring suit within four years after the qualified disposition was made or, if later, within one year after the creditor discovered (or should have discovered) the qualified disposition. If a creditor's claim under the Delaware Uniform Fraudulent Transfers Act arose concurrent with or subsequent to the qualified disposition, the creditor must bring suit within four years after the qualified disposition was made. A creditor must prove by clear and convincing evidence that such transfer was fraudulent.

TOTAL RETURN UNITRUSTS

To provide solutions to trustees of trusts administered in Delaware or governed by Delaware law desiring to invest trust assets for total return while balancing the interests of current and remainder beneficiaries, Delaware has enacted legislation (i) providing a trustee with certain powers to adjust between income and principal, along with the ability to seek an advance determination from the Court of Chancery that a proposed power of adjustment will not constitute an abuse of the trustee's discretion, and (ii) as set forth in detail below, permitting a trustee to pay a unitrust amount based on a percentage of the value of the trust as opposed to an income amount to current beneficiaries.

In 2001, Delaware became the first state to enact a total return trust statute. Under the Delaware statute, a trustee may convert an income trust to a unitrust, reconvert a unitrust to an income trust, or change the percentage used to calculate the unitrust amount and/or the method used to determine the fair market value of the trust. In addition, under Delaware's express total return unitrust statute, a trust instrument expressly drafted to provide for the payment of a unitrust amount may be converted to an income trust or may change the percentage used to calculate the unitrust amount pursuant to the mechanism provided under the total return trust statute. Under the total return trust statute, one procedure applies if the trustee is a disinterested trustee, and another procedure applies if there is an interested trustee. A unitrust payout allows the trustee to pay a specified percentage of the fair market value of the trust annually to the current beneficiary (rather than just the income from the trust), thereby affording the trustee greater investment flexibility and protection under Delaware's prudent investor rule.

A disinterested trustee may convert an income trust to a unitrust without court approval if it adopts a written policy, satisfies notice requirements, and does not receive written objections. Notice of the proposed conversion must be sent to (i) the trustor, if living, (ii) all living persons who are currently receiving or are eligible to receive income distributions, (iii) all living persons who would receive principal if the trust were then terminated, and (iv) all advisors or protectors. At least one current income beneficiary and one contingent remainderman must be legally competent in order for the notice to be effective under the statute.

An interested trustee may convert an income trust to a unitrust without court approval if the policy, notice, and objection requirements described above are satisfied and if it appoints a disinterested person to determine the unitrust per-

centage and related matters in a fiduciary capacity. The trustee's notice must contain the disinterested person's determinations.

A trustee may always petition the Court of Chancery for guidance if it is unable to convert the trust to a unitrust under the above procedures, either because a beneficiary objects or because a competent beneficiary is not in the current or next generation. Subject to the terms of the trust instrument, the trustee may decide the effective date of the conversion, the timing of distributions, whether distributions will be made in cash or in kind, and certain other administrative issues. Under the Delaware statute, the trustee is not personally liable if it makes the wrong decision. Procedures and computer software have been developed to implement the statute.

The Delaware statute provides that conversion of a trust to a total return unitrust is a matter of trust administration and that the statute is available to certain trusts whose governing instrument provides that Delaware law governs its construction and administration and to trusts administered in Delaware under Delaware law. Thus, if moving a trust results in a change in the law that governs its administration to Delaware law (either pursuant to the terms of the trust instrument or specific language in a court order), the trust will be able to take advantage of the statute.

PRIVATE FOUNDATION LAWS AND PROCEDURES

Most states have addressed issues of nonprofit corporate governance through the adoption of separate nonprofit corporation acts. Although Delaware has not adopted a separate nonprofit corporation act, recent amendments to the General Corporation Law of the State of Delaware have, in effect, created a specific body of law for nonprofit corporations by applying (with appropriate modifications) Delaware's for-profit corporation laws to such corporations. In addition, Delaware case law indicates that principles of corporate law, as opposed to trust law principles, will determine whether the directors of Delaware nonprofit corporations have met their fiduciary obligations.

Most state nonprofit corporation acts do not provide a general standard of care applicable to the directors of nonprofit corporations and do not provide clear guidance that the duties of such directors are similar to those of their for-profit counterparts. Even in the few states where there is no separate nonprofit corporation act, distinctions may still be drawn between the fiduciary duties of directors of nonprofit corporations and the fiduciary duties of directors of for-profit corporations. In many states, further case law development has been

and will be required to clarify the extent to which corporate rather than trust law principles will apply.

A donor should consider creating his private foundation as a Delaware non-profit corporation because Delaware law provides clear guidance on the fiduciary duties applicable to directors, flexible standards of corporate governance, and minimal governmental interference with the activities of charitable entities. (See Chapter Two, “**Business Entities – Corporations – Membership Corporations.**”)

CHAPTER TWELVE

ADMINISTRATIVE LAW AND REGULATION OF STATE AGENCIES



**Delaware administrative laws balance the need for
regulation with an efficient economy.**

Delaware state government provides an array of services to its citizens and others having contact with the State. In 1969, Delaware adopted a cabinet form of government reorganizing many boards and commissions of the State that had existed for decades into a more streamlined governmental system. Each cabinet department is headed by a cabinet secretary. Major cabinet departments include the Economic Development Office, as well as the Departments of Transportation, Safety and Homeland Security, Health and Social Services, Correction, Labor, Natural Resources and Environmental Control, Agriculture, Children, Youth and Their Families, Technology and Information, Finance, and State. Each state department is typically divided into various divisions, each headed by a division director. The division directors generally report to the cabinet secretary.

Delaware also has certain ancillary agencies, boards, and commissions not part of the cabinet departments or only loosely affiliated with cabinet departments. Major ones include the Public Service Commission, the State Bank Commissioner, the Board of Education, the Election Commissioner, the Compensation Commission, the Human Relations Commission, the Public Defender, the Office of the Child Advocate, and numerous boards and commissions regulating professions and other matters.

Certain Delaware offices created by the Delaware Constitution remain independent within the executive branch of government. These include the Attorney General, the Insurance Commissioner, the Auditor of Accounts, and the State Treasurer.

Reflective of the State's small size, government in Delaware has broader responsibilities than in most states. For example, unlike many states, Delaware's education system operates at the state level and is not a county or municipality service. Similarly, corrections, prisons, welfare, roads, highways, transportation, and criminal prosecution are all handled by state-level agencies. As a result, in comparison to other states, Delaware's state operating budget (including the elementary and secondary education budget and the highway budget) is higher on a per capita basis than in most states.

All state agencies and departments, and most boards and commissions, have the power to issue rules and regulations necessary for their respective operations, to enforce such rules and regulations, and otherwise to manage operations consistent with the broad purposes of Delaware law. Most state agencies, in the adoption of rules and regulations and in decisions involving potential violations, are generally subject to the Delaware Administrative Procedures

Act. However, certain agencies, including the General Assembly, the courts, municipalities, and other political subdivisions and school districts, are not subject to that Act. Generally, the Administrative Procedures Act provides a framework and guidelines for the adoption of rules and regulations by state agencies, boards, and commissions, and procedures for deciding case decisions. Parties aggrieved by a case decision of a state agency generally may, under certain circumstances, appeal for relief to the Superior Court of the State of Delaware. Appeals of case decisions are on the record without a trial *de novo*.

The Division of Research was created by the General Assembly and charged with compiling, maintaining, and publishing monthly the Register of Regulations of the State of Delaware. The registrar of regulations is an employee of the Division of Research of the General Assembly and is charged with the day-to-day responsibility of maintaining the Register of Regulations. The registrar has the power and responsibility to require all state agencies to submit copies of proposed regulations to the registrar as well as subsequent amendments, repeals, and additions. The registrar also has the power and authority to advise agencies as to the form and style of the regulations in order to provide some general uniformity.

State agencies generally are also subject to Delaware's Freedom of Information Act. The Freedom of Information Act designates certain records as public records and provides for their general availability to the public. The Freedom of Information Act also generally requires open meetings for most state agencies, boards, and commissions. However, neither the General Assembly of the State of Delaware nor any caucus thereof or committee or subcommittee is subject to the Freedom of Information Act. Also exempt from the provisions of that Act are the University of Delaware and Delaware State University, except for the boards of trustees of those educational institutions. The Freedom of Information Act provides that certain records are not deemed public records and are therefore not generally available to the public, including medical records, student records of educational institutions, trade secrets, criminal or civil investigatory files, criminal or civil records, intelligence files by law enforcement agencies, records that disclose the identity of contributors to charitable organizations, records involving labor and collective bargaining negotiations, inmate records of the Department of Corrections, and investigative files maintained by the Violent Crimes Compensation Board.

The open-meeting provisions of the Freedom of Information Act generally require prior notice of meetings, their agendas, and the ability of individual cit-

izens to attend and present views. Under certain circumstances, a public body may hold an executive session closed to the public, but formal votes on public business are not allowed in executive sessions. The open-meetings provisions of the Delaware Freedom of Information Act do not apply to grand juries, petit juries, special juries, the Board of Pardons and Parole, or the Violent Crimes Compensation Board, or the deliberations of the State Human Relations Commission, the Industrial Accident Board, and the Tax Appeals Board involving case decisions.

Delaware also provides a detailed scheme of regulation for the delivery of services to Delaware citizens by organizations deemed to be monopolies. In Delaware, the regulation of such entities is the responsibility of the Public Service Commission. The Public Service Commission has five members appointed by the Governor and confirmed by the Senate, has a full-time staff, and is housed within the Department of State. The Delaware Public Service Commission generally regulates the provision of electrical services, natural gas, telephone service, and water services, and has certain responsibilities with respect to the regulation of car dealerships and a limited role in the regulation of cable television services.

In administering the laws of Delaware, state employees, officers, and officials are subject to the State Employees', Officers' and Officials' Code of Conduct. The Code of Conduct was enacted to help ensure propriety and to preserve the public's confidence and trust in public employees, officers, and officials. Generally, the Code of Conduct prohibits conflicts of interest, requires certain financial disclosures, and creates the State Public Integrity Commission to issue and enforce rules with respect to the Code of Conduct.

CHAPTER THIRTEEN

PRINCIPAL ECONOMIC DEVELOPMENT AND BUSINESS ASSISTANCE AGENCIES

**Agencies and organizations providing assistance to
businesses are readily accessible.**

Set forth below are addresses and contact numbers for economic development agencies, Chambers of Commerce, and other organizations that provide assistance to persons seeking to establish businesses in Delaware.

ECONOMIC DEVELOPMENT AGENCIES

Delaware Economic Development Office

99 Kings Highway • P.O. Box 1401 • Dover, Delaware 19901
(302) 739-4271 • (302) 739-5749 (fax) • dedo.delaware.gov

Kent Economic Partnership

435 N. DuPont Highway • Dover, Delaware 19901
(302) 678-3028 • (302) 678-0815 (fax) • kentpartnership.org

New Castle County Economic Development Council

12 Penns Way • New Castle, Delaware 19720
(302) 294-2058 • (302) 322-3593 (fax) • nccedc.com

Wilmington Office of Economic Development

Louis L. Redding City/County Building • 800 North French Street, 3rd Floor
Wilmington, Delaware 19801
(302) 576-2120 • (302) 571-4326 (fax)
ci.wilmington.de.us/departments/economic.htm

Sussex County Department of Economic Development

21553 Rudder Lane • P.O. Box 589 • Georgetown, Delaware 19947
(302) 855-7770 • (302) 855-7793 (fax) • sussexcounty.net/dept/econdev

STATE GOVERNMENT OFFICES

Delaware Department of State

Townsend Building • 401 Federal Street, Suite 3 • Dover, Delaware 19901
(302) 739-4111 • (302) 739-3811(fax) • sos.delaware.gov

Delaware Division of Corporations

Townsend Building • 401 Federal Street, Suite 4 • Dover, Delaware 19901
(302) 739-3073 • (302) 739-3812 (fax) • corp.delaware.gov

Delaware Insurance Department

841 Silver Lake Boulevard • Dover, Delaware 19904
(302) 674-7300 • (302) 739-5280 (fax) • delawareinsurance.gov

Office of the State Bank Commissioner

555 E. Loockerman Street, Suite 210 • Dover, Delaware 19901
(302) 739-4235 • (302) 739-3609 (fax) • banking.delaware.gov

Division of Revenue

Carvel State Office Building • 820 North French Street
Wilmington, Delaware 19801
(302) 577-8200 • (302) 577-8202 (fax) • revenue.delaware.gov

CHAMBERS OF COMMERCE AND OTHER ORGANIZATIONS

Delaware State Chamber of Commerce

1201 North Orange Street, Suite 200 • P.O. Box 671
Wilmington, Delaware 19899-0671
(302) 655-7221 • (302) 654-0691 (fax) • dscc.com

New Castle County Chamber of Commerce

12 Penns Way • New Castle, Delaware 19720
(302) 737-4343 • (302) 322-3593 (fax) • ncccc.com

Central Delaware Chamber of Commerce

435 North DuPont Highway • Dover, Delaware 19901
(302) 734-7513 • (302) 678-0189 (fax) • cdcc.net

Greater Georgetown Chamber of Commerce

140 Layton Ave. • P.O. Box 1 • Georgetown, Delaware 19947
(302) 856-1544 • (302) 856-1577 (fax) • georgetowncoc.com

The Committee of 100

704 North King Street, Suite 512 • Wilmington, Delaware 19801
(302) 654-6115 • (302) 654-1556 (fax) • committeeof100.com

Delaware Small Business Development Center Network

University of Delaware • Delaware Technology Park
1 Innovation Way, Suite 301 • Newark, Delaware 19711
(302) 831-0770 • delawaresbdc.org

Delaware Service Corporation of Retired Executives

The Nemours Building • 1007 Orange Street, Suite 1120
Wilmington, Delaware 19801
(302) 573-6552 • (302) 573-6092 (fax) • delaware.score.org

Small Business Administration

Delaware District Office • 1007 North Orange Street, Suite 1120
Wilmington, Delaware 19801
(302) 573-6294 • sba.gov/about-offices-content/2/3107

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