



Morgan Lewis

DELAWARE DGCL AMENDMENTS – SB 21

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Background: Why the Amendments?

- Uncertainty & Perceived Unfairness = Threat to Delaware's Dominance
- 2024 was eventful year in controlling shareholder transactions
 - *Moelis*: voided shareholder agreements – upended longstanding, pervasive practice
 - *Match*: *MFW* applies to ALL controlling shareholder transactions
 - *Tornetta/Musk*: Highlighted ambiguity as to who is a controlling shareholder
- Delaware Responds With Amendments
 - Section 144
 - Conflicted Director Transactions
 - Controlling Stockholder Transactions
 - Section 220: Stockholder's Right to Inspect Books and Records

Why it Matters: Standard of Review

Business Judgment Review

Decisions by disinterested and independent directors are subject to the business judgment standard of review

- Decisions made in good faith and with due care will not be second guessed
- Plaintiffs bear the burden of pleading waste or egregiousness

Entire Fairness Review

- Applies when a majority of the board is conflicted, or a controlling stockholder either stands on both sides or receives “nonratable” benefits
- Defendants bear the burden to prove:
 - Fair process/Fair price
- Where entire fairness applies, pleading stage motions to dismiss are rarely granted
- The case will likely either settle or go to trial (summary judgment is rare)

Conflict of Interest Transactions – Section 144

Conflict of Interest Transactions (other than controlling stockholder)

- Old Section 144 -- “Safe Harbor”
 - Applied where directors were interested in transaction
 - Approval of transaction by disinterested directors or stockholders upon disclosure of conflict rendered transaction not void or voidable solely due to conflict
 - Conflicting judicial decisions as to whether compliance with safe harbors meant business judgment review or merely shifts burden on entire fairness
- New Section 144 – “Much Safer Harbor”
 - Approval (*in good faith*) by board or committee so long as majority of disinterested directors; or
 - Approval or ratification by disinterested stockholders
 - Approval of transaction by disinterested directors or stockholders upon disclosure of material facts means ***no equitable relief or damages based on conflict, period.***

Controlling Stockholder Transactions – New Section 144

Fewer Circumstances Under Which Minority Stockholders Deemed Controllers

- **Defines “controlling stockholder” (narrower than common law)**
 - (a) owns or controls a majority of voting stock (50% +) entitled to vote in director elections, or
 - (b) has the right to select and cause the election of nominees constituting a majority of the board, or
 - (c) has equivalent power to appoint directors with majority voting power by holding at least one-third (33%) of the corporation’s voting stock and has managerial authority over the business and affairs of corporation.
- **Defines “control group” (consistent with common law)**
 - Two or more persons who, through an agreement or arrangement, collectively act as a controlling stockholder.
- **Defines “controlling stockholder transactions” (consistent with common law)**
 - Those where a controller: (i) stands on both sides or (ii) receives benefits not shared with other stockholders.

Controlling Stockholder Transactions – New Section 144 (Other Than “Going Private” Transactions)

Conflicted Transaction Safe Harbors

- Conflicted transactions (**other than going-private transactions**) now have a safe harbor barring both equitable relief and damages if transactions are *either*:
 - (a) approved by fully informed committee of at least two disinterested directors, **or**
 - Only majority of disinterested directors “then serving” is required (MFW/Match required all directors serving on the committee be disinterested)
 - (b) approved or ratified by a majority of the votes cast (MFW required votes outstanding) by the corporation’s disinterested stockholders (and conditioned on such approval prior to submission to stockholders).
 - Must be fully informed vote
 - No coercion
- No *ab initio* requirement

Controlling Stockholder Transactions – New Section 144 (“Going Private” Transactions)

- **Going Private Transactions**: Must still comply with **both** committee approval and stockholder approval for going private transactions (see previous page)
 - For public companies with shares registered under the '34 Act or listed on an exchange, going private transaction is defined with reference to Rule 13e-3 transactions
- *MF*'s dual requirements only required for going-private transactions
 - Overrules *In re Match.com*
- **Satisfaction of applicable safe harbors means no equitable relief or damages based on conflict**

Controlling Stockholder Transactions – New Section 144

More Certainty Regarding Director Independence

- **Presumption of independence** for directors who are not a party to a transaction and who have been deemed independent under rules of the stock exchange on which the corporation's common stock is listed
 - Presumption can only be rebutted by "substantial and particularized facts"
- **Defines "disinterested director"** as one who is not a party to a transaction, lacks a *material* interest in it, and has no material relationship with anyone who does
 - "Material interest" and "material relationship" are narrowly defined

Books & Records: Amended Section 220

- **Old 220**

- Did not define “books and records” – scope developed by common law
- Often included formal board materials and informal documents (emails and text messages)
- Section 220 demands became increasingly costly and burdensome

- **Amended 220**

- Specifies “Books and Records” (formal board materials, financials, *Moelis* agreements, director independence questionnaires, etc.)
- Allows production of emails and texts only in narrow exceptions
- Codifies protections of confidentiality, redaction of nonresponsive information and “incorporation by reference” condition

Books & Records: Amended Section 220

- Formal board materials/minutes are presumptively the scope unless exceptions are met:
 - (1) Corporation does not maintain “books and records”
 - “functional equivalent” of records if necessary and essential to purpose
 - (2) Emails/texts if Stockholder demonstrates:
 - a “compelling need” to inspect such records to further the stockholder’s proper purpose, and
 - demonstrates by *clear and convincing evidence* that such specific records are “necessary and essential” to further such purpose.

Books & Records: Amended Section 220

- Practical Implications
 - Transactions
 - Litigation
 - Corporate Recordkeeping and Board Minutes

Where Do We Go From Here?

- Court of Chancery will likely interpret Amendments narrowly
- Plaintiffs' Bar is creative – new issues will emerge
- Ambiguities and litigable issues remain
 - Whether stockholder with 33% -50% acts with managerial control
 - Whether stock exchange independence definitions now get litigated
 - Whether committee acted in good faith
 - Uncertainty around Rule 13e-3 transactions
 - Whether stockholder vote was fully informed
 - *In re Sears* –potential fiduciary liability for controllers exercising right to vote
 - Aiding and abetting liability

DExit?

- Alternative jurisdictions have adopted business statutes that are more D&O friendly
- Statutes do not enforce themselves
- The value provided by Delaware is judicial expertise
- There is a reason Nevada includes the following in its corporations statutes:

The plain meaning of the laws enacted by the Legislature in this title, including, without limitation, the fiduciary duties and liability of the directors and officers of a domestic corporation set forth in NRS 78.138 and 78.139, must not be supplanted or modified by laws or judicial decisions from any other jurisdiction.

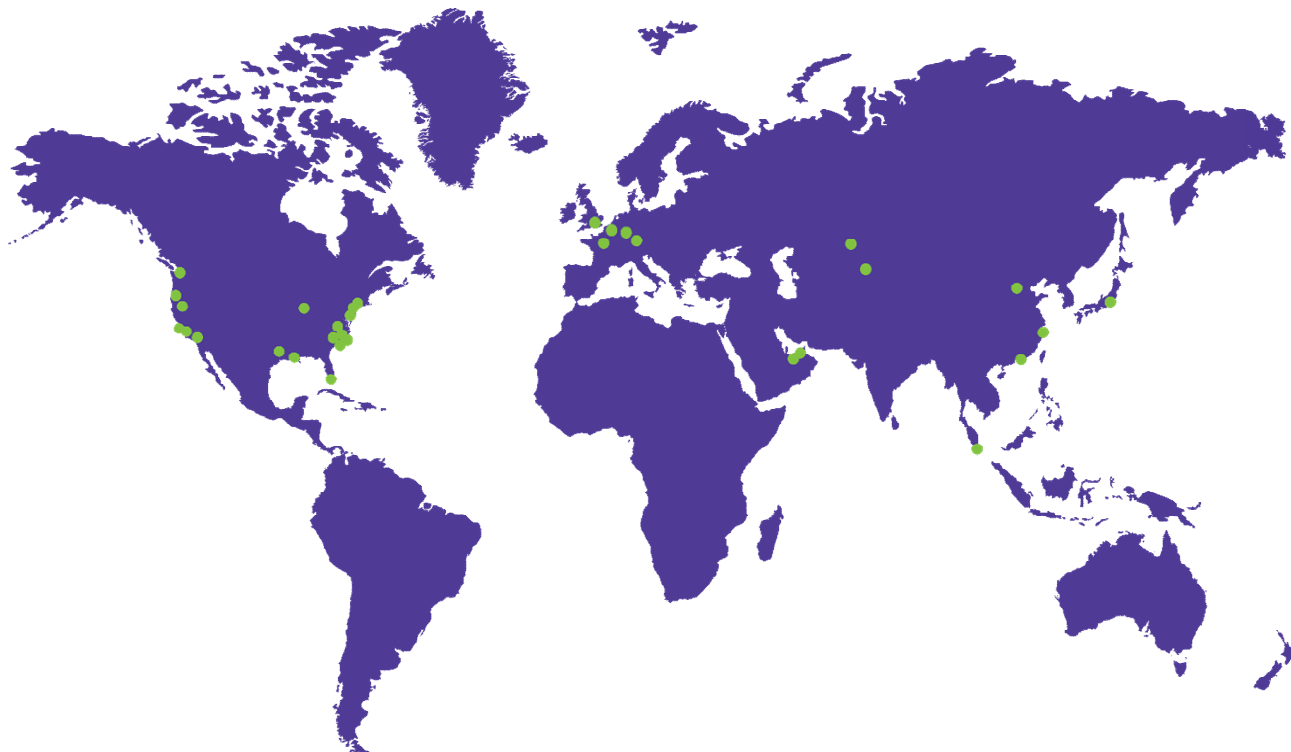
NV ST 78.012(3)

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