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Rethinking Delaware Forum Bylaws In Light of Disclosure-Only Settlements

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There are many good reasons, which will not be repeated here, for Delaware corporations, especially public companies, to adopt so-called Delaware-forum bylaws. These provisions, which have been upheld by courts in at least eight states and counting, establish the Delaware Chancery Court as the exclusive venue for stockholder claims and other actions involving the corporation's internal affairs. Many of these bylaw provisions were adopted prior to the decision in *In re Trulia Stockholder Litigation*[1] in which the Delaware Chancery Court expressed its "disfavor" of "disclosure-only" settlements in M&A litigation, except in rare situations where the supplemental disclosures pursuant to the settlements "significantly alter the total mix of information made available" to stockholders.

While the *Trulia* decision seems to have reduced the incidence of M&A derivative claims, when such claims are asserted a disclosure-only settlement and broad release of the stockholder claims may no longer be available to the corporation and its directors even if they would prefer a disclosure-only settlement to avoid settlement payments in cash or stock. Moreover, waiving the Delaware-forum bylaw may not be an effective option. We are aware of at least one stockholder derivative action filed in the U.S. District Court for the Central District of California against the directors of a Delaware corporation in which the plaintiffs and the defendant agreed to a disclosure-only settlement only to have the Court refuse to approve it where the corporation's board of directors had waived the corporation's Delaware-forum bylaw in order to facilitate the settlement. Although the procedural aspects of the case were awkward, the Court was apparently unwilling to approve the settlement where it appeared to be inconsistent with the law of Delaware, which the Court concluded was the proper forum for the case. The plaintiffs in the case subsequently filed an identical action in the Delaware Chancery Court, and plaintiffs in a competing derivative action pending in Delaware have alleged that the board of directors of the corporation breached their fiduciary duty by waiving the Delaware-forum bylaw provision to accommodate the plaintiffs in the dismissed California derivative action.

In other states, including California, presumably, disclosure-only settlements may still be viable. On February 2, 2017, for example, a New York appellate court approved a disclosure-only settlement in *Gordon v. Verizon Communications, Inc.* *(http://www.nycourts.gov/reporter/3dseries/2017/201700742.htm).* In doing so, the Appellate Division, First Department, articulated a five-factor test for approval of disclosure –only settlements under New York law that is seemingly less stringent than the test under *Trulia*.

Supermajority Stockholder Approval Bylaw

The Delaware Chancery Court ruled recently that a bylaw requiring a supermajority (66-2/3%) stockholder vote to remove directors was invalid under Delaware law, because it was inconsistent with Section 141(k) of the Delaware General Corporation Law (DGCL). Section 141(k) provides that, except with respect to corporations having a classified board or

1 129A.3d 884 (Del. Ch. 2016)

cumulative voting for directors, any director may be removed with or without cause by a majority stockholder vote. Section 141(k) does not allow for exceptions to this requirement in a bylaw provision; however, the same supermajority stockholder vote provision would be valid if set forth in the corporation's certificate of incorporation in light of Section 102(b)(4) of the DGCL, which permits a certificate of incorporation to include supermajority voting provisions.

We recommend that clients review their bylaws for any voting requirements for the removal of directors or other actions that would be inconsistent with Section 141(k) or other section of the DGCL. Presumably, a bylaw providing that directors may be removed by stockholder vote only for "cause" also would be invalid under Section 141(k).

Say-on-Pay Frequency

Since 2011, public companies have been required to conduct a stockholder advisory vote, or "say-on- pay vote," on the compensation of the companies' "named executive officers," as well as an advisory vote on whether the say-on-pay vote should be conducted every one, two or three years. This latest advisory vote is referred to as the "say-on-frequency vote."

As a reminder, public companies are required to conduct the say-on-frequency vote "no later than the annual or other meeting of shareholders held in the sixth calendar year after the immediately preceding vote," which for most companies that were public in 2011 will be in 2017.

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If you would like to know more about these matters, please contact the TroyGould PC corporate attorney with whom you regularly work or any of our Corporate Department attorneys.