RESOURCE DOCUMENT ON DELAWARE CORPORATION LAW

BY THE GENERAL CORPORATION LAW COMMITTEE OF THE DELAWARE STATE BAR ASSOCIATION

INTRODUCTION

FOR SOME TIME now certain legal scholars¹ and others² have been sharply criticizing Delaware and its General Corporation Law. These critics' perceptions of Delaware corporation law differ from that of lawyers both in Delaware and elsewhere who work daily with that law.

This document is the work of a subcommittee of the Delaware State Bar Association's General Corporation Law Committee. It sets out, by illustration from existing cases, statutes and other authorities, certain substantial equitable principles underlying the Delaware corporation law, as well as remedies for its violation.

We believe that the Delaware legislature and courts do not lean over backward to assist and defend management; nor do they show undue partiality to the interests of the creditor, shareholder or the government. A fair analysis of Delaware corporation law shows it to be firmly rooted in equitable principles and administered by knowledgeable courts. Once in court the facts of the case, the law, and the court's conscience have in the past, and very likely will in the future, determine the result.

I. Stockholder Control

a. Introduction

The ultimate private source of control of the corporation is the body of stockholders. This control is brought to bear by the election

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of directors and major corporate changes, if any, at regular and special stockholders meetings. Directors can be changed in whole or in part either by the stable body of stockholders or, after a change of control, by the new group of stockholders which has replaced the old. Stockholders can also act instantly through written consents by holders of that percentage of stock required by the law or the certificate of incorporation to authorize the act in question.3

b. Annual Meeting

To guarantee that the stockholders' franchise is honored, the directors, and therefore management, must face the stockholders at least once a year. Efforts of management to avoid this confrontation have met with little success. Annual meetings to elect directors are required by statute.4 The courts are firm that postponement of this requirement will not be permitted. Vice Chancellor Brown recently wrote:

[T]he spirit of 8 Del. C. § 211(c) indicates that where more than thirteen months have elapsed without a meeting of shareholders to elect directors and application is made by a shareholder for Court intervention because of this, the Court has a duty to make sure that such a meeting and election take place as promptly as possible, and normally this can only be guaranteed by the entry of an order fixing a definite date for the event to take place.5

Nor have the courts been charitable to a management which, without proper business reasons, would use the literal language of the statute to alter the meeting date. When such an effort was made to rush competitors for control unprepared to a meeting earlier than they had reason to expect, Justice (now Chief Justice) Herrmann roundly condemned the practice: "Management contends that it has complied strictly with the provisions of the new Delaware Corporation Law in changing the by-law date [for the annual meeting]. The answer to that contention, of course, is that inequitable action does not become permissible simply because legally possible."6

3. 8 Del. C. §§ 211, 222, 228(a). See note 10 infra.
On the other hand, dissidents were held to an annual meeting date of which they had been on notice for some time, and a delay in an annual meeting inadvertently, or at least not inequitably, brought about was not condemned since the meeting had been promptly rescheduled.\(^7\)

c. **Consents**

Direct stockholder control was legislated in 1967 through section 228(a) which allows a corporation to dispense altogether with an actual meeting of stockholders and permits them to act by written consent. This section, together with the provision for removal of directors without cause,\(^8\) permits immediate and direct control by the majority of the stockholders (followed by full disclosure to the entire body of shareholders) including, where appropriate, the ouster of management.\(^10\)

II. **Stockholders’ Rights to Information**

a. **Inspection of Stockholders’ Lists**

No state grants stockholders a broader right to a list of fellow stockholders than does Delaware. *General Time Corp. v. Talley Industries, Inc.*, held that if the plaintiff was a shareholder and his purpose was germane to that position, he was entitled to the list. Chief Justice Wolcott wrote:

> In short, we are of the opinion that when a stockholder establishes his status as such, and seeks production of a stockholders’ list for a purpose germane to that status, such as a proxy solicitation, he is entitled to its production.

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8. *In re Tonopah United Water Co.*, 139 A. 762 (Del. Ch. 1927) (an error in the notice for the proper date made the meeting of questionable validity, therefore, a later date was acceptable).

9. 8 Del. C. § 141(k).

10. Cary, *Federalism Article* at 669, considers section 228, which grants direct control to the majority of shareholders, somehow anti-democratic because the procedure provides disclosure to the minority only after the fact. First, speed is often desirable. Second, the proxy rules and Delaware law require disclosure before the fact if consents are solicited. Third, section 228(c) requires full disclosure after the fact in every case. It is true that the consent procedure balances the interest of prompt action, when necessary votes are in hand, against a lost opportunity for a preliminary injunction if no solicitation is required. However, abuses are subject to correction by judicial review; see, e.g., Chew v. Inverness Management Corp., 352 A.2d 426 (Del. Ch. 1976). When the majority stockholder or stockholders determine corporate policy they become fiduciaries in relation to all of the stockholders, just as directors are. Allied Chemical & Dye Corp. v. Steel & Tube Co., 120 A. 486 (Del. Ch. 1923); Epstein v. Celotex Corp., 238 A.2d 843 (Del. Ch. 1968); David J. Green & Co. v. Dunhill Int’l, Inc., 249 A.2d 427 (Del. Ch. 1968); Trans World Airlines, Inc. v. Summa Corp., No. 1607 (Del. Ch. March 25, 1977), *rearg. denied* (Del. Ch. May 10, 1977).
It might well be asked what circumstances then would constitute a defense to the demand. Each case must depend upon its particular facts, but we point out that in the Theile case an individual owning one share of stock was denied a list when it appeared that his purpose was to sell it for a "sucker list." 11

This position was not novel in 1968 when General Time was decided. The Chief Justice cited a case from the 1920s 12 in support of the proposition that "the desire to solicit proxies for a slate of directors in opposition to management is a purpose reasonably related to the stockholder's interest as a stockholder." 13

The opposition to legitimate list production is now simply a delay tactic which the courts have thwarted by requiring an expedited trial on the merits, often within ten days of the complaint, if the need can be demonstrated. 14

Defenses have fallen right and left. If one purpose is proper, it is irrelevant that another may not be. 15 Lack of SEC approval for the materials to be mailed is irrelevant. 16 Indeed, it is no bar to production of the list that one purpose of the stockholder may be to use the list to violate the securities laws. 17 It is irrelevant that the stockholder buys his shares just so he can demand the list; 18 and the fact that litigation is pending elsewhere where the list demand might have been made, in discovery for instance, is no defense. 19

Therefore, the short answer in stock list cases is, if a stockholder in a Delaware corporation has a purpose relevant to that status, be it for solicitation of proxies or tender offers, he may get the stockholders' list as promptly as needed. Indeed, management's

12. State ex rel. Theile v. Cities Service Co., 115 A. 773 (Del. 1922). This right is so clear that, before jurisdiction was granted to the Court of Chancery in 1967, the list was obtained as of right, by the use of a writ of mandamus.
13. 240 A.2d at 756. Some cases have held that the corporation is entitled, however, to a specification of purpose beyond mere expression of a desire to confer with other stockholders, e.g., Northwest Indus. v. B.F. Goodrich Co., 260 A.2d 428 (Del. 1969); Weisman v. Western Pac. Indus., Inc., 344 A.2d 267 (Del. Ch. 1975).
14. In tender offer cases the time has been even shorter.
attempt to delay a dissident by compelling him to copy stock ledger cards by hand may be thwarted by an order directing that a computer tape be furnished.\textsuperscript{20}

b. Inspection of Books and Records

As a general proposition, the Delaware law recognizes a stockholder’s interest in accessibility to corporate information. Once a meritorious suit is brought, in Delaware at least, wide access to corporate information is available. Delaware trial courts have adopted rules of civil procedure identical to the federal model in nearly all respects. In discovery matters the rules are read liberally, allowing both plaintiff and defendant full examination of their adversaries’ books and papers which are not privileged and “appear reasonably calculated to lead to the discovery of admissible evidence.”\textsuperscript{21}

But what about before suit, when the stockholder has a legitimate question about a transaction he has cause to think unsavory? Long before the federal rules a Delaware stockholder, for a proper purpose and at reasonable times, had a broad right to review the books and records of his company.\textsuperscript{22} Chief Justice Pennewill in \textit{State ex rel. Cochran v. Penn-Beaver Oil Co.}, in granting a preemptory writ of mandamus permitting such inspection, wrote:

Under the common law a stockholder had the right to examine the books and records of the company, and that right could not be taken away except by a statute that expressly or by necessary implication authorized it. There is no such statute, and we conclude that the provision in the certificate of incorporation of defendant company, under which the relator was denied the right to inspect the company’s records, forms no part of its charter and should be disregarded.\textsuperscript{23}

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\ldots The extent and scope of the privilege granted must depend in a large degree upon the company’s treatment of the relator’s legitimate request, and the extent to which the


\textsuperscript{23} 143 A. 257, 259 (Del. Ct. in Banc 1926).
company has furnished to its stockholders, by financial statements and otherwise, information relative to the conduct and condition of its business. The stockholder is entitled to reasonable information from his company along this line, and we do not think it would be ordinarily denied. 24

A books and records review is a powerful and appropriate weapon to investigate improper transactions. As Chief Justice Southerland wrote in Nodana Petroleum Corp. v. State ex rel. Brennan: "[W]e find that plaintiff did sufficiently state the purpose of his inspection, i.e., the investigation of improper transactions. The corporation appears to admit that this is a proper purpose; at all events we have no doubt about it." 25

Unlike stock list cases where the burden of proving improper purpose falls on the company, the burden of such proof in a books and records case falls on the plaintiff. Additionally, the plaintiff must need such relief. In a recent case, the Chancellor noted that if the stockholder is litigating against the corporation in another court and has the means in the other court to require inspection of books and records, such factor would be considered in determining the propriety of the stockholder's purpose. 26 If, however, the stockholder has no such means in the other litigation, the pendency of litigation elsewhere is no more a defense than it would be in a stock list case. 27

The stockholder's right to access is not unlimited however. The Delaware courts recognize that the stockholder, being under no fiduciary duty to the corporation as such, may misuse confidential information to the detriment of the corporation itself. Under such circumstances access will be denied. 28

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24. Id. at 260. Delaware, like other states, permits neither the satisfaction of idle curiosity, Insurashares Corp. v. Kirchner, 5 A.2d 519 (Del. 1939); nor harassment, State ex rel. Brumley v. Jessup & Moore Paper Co., 77 A. 16 (Del. 1910). As the court in the Cochran case said: "While it is the duty of the court to protect the rights of stockholders, it is equally their duty to safeguard the rights of the corporation as such." 143 A. at 260.

25. 123 A.2d 243, 246 (Del. 1956) (emphasis supplied).


Nonetheless, upon balance, the stockholder’s right to inquire into the affairs of his company and to communicate with fellow stockholders is as broad in Delaware as anywhere in the country.

c. Proxy Materials

Using the concepts of common law fraud, Delaware courts have repeatedly condemned misleading proxy solicitation. Three cases, one in which dissidents were enjoined and two in which management was enjoined, will serve to illustrate the approach of Delaware courts.29

In Empire Southern Gas Co. v. Gray,30 the corporation sought to enjoin a dissident faction of officers from soliciting proxies by a statement which appeared to, but did not, come by authority of the directors. The court placed “the burden of candor” on the solicitor of proxies and enjoined the use of the misleading material. The court’s statement of the law is as valid today as it was then:

Would a stockholder reading the notice, the proxy statement and the proxy be likely to obtain the impression that the proxy was being solicited by authority of the board of directors of the complainant company? I believe that he would so conclude, unless it is to be implied that the law will assume each stockholder will read and examine the various documents through the eyes of one who is placed on guard as to the possible existence of misleading statements. To expect or to require such a procedure of stockholders would remove the law beyond reason or reality. The accepted and desirable tendency has been to place the burden of candor upon those who would communicate with stockholders rather than to require the stockholders to be eternally vigilant.31

29. There is a heavy equitable flavor to Delaware cases in this area as well. In In re Seminole Oil & Gas Corp., 150 A.2d 20 (Del. Ch. 1959), for example, the court found both management and dissidents guilty of material misstatements; the misrepresentations were offsetting and the court declined to impose the economic burden of resolicitation on a small corporation.

30. 46 A.2d 741 (Del. Ch. 1946). The Empire Southern case turned aside an argument that a review of the corporate election thus tainted was the sole remedy for proxy fraud. Both remedies exist side by side.

31. Id. at 746. Equally instructive are the cases which, after carefully weighing all the evidence including the motives of the parties, have found no material misrepresentation to require that the proxy materials be condemned, e.g., Saxe v. Brady, 184 A.2d 602 (Del. Ch. 1962); Lynch v. Vickers Energy Corp., 351 A.2d 570 (Del. Ch. 1976); American Hardware Corp. v. Savage Arms Corp., 135 A.2d 725 (Del. Ch.), aff’d, 136 A.2d 690 (Del. 1957).
In Gerlach v. Gillam, certain stockholders of United Printers & Publishers, Inc., sought to enjoin the consummation of transactions which would have personally benefited the corporation’s dominant director. The stockholders had ratified the transaction, thus management argued that the claim for injunctive relief was precluded. The court disagreed, finding that ratification had been based on a false and misleading proxy statement which had failed to disclose the dates of the challenged contracts, how they were negotiated, and the dominant director’s role in their negotiation. The court let its previous interlocutory injunction stand.

In Campbell v. Loew’s, Inc., Loew’s president had solicited proxies which he sought to use to remove certain directors for cause. The proxy materials had presented only the case for removal and the directors under attack had been denied a stockholders’ list to use in reply. Finding that stockholders had been deprived of the opportunity to hear both sides, the Chancellor ruled the proxies invalid for use on the removal question. However, following a detailed review of the specific and cumulative effect of a number of claimed misrepresentations together with the “whole impact . . . the proxy material conveyed to the average reader,” the court declined to invalidate the proxies for other purposes.

Delaware courts are barred by federal law from taking jurisdiction over violations of federal proxy rules. The substantial result, however, is less than meets the eye. Twenty years ago, in the context of an election review, Vice Chancellor Seitz pointed out that violations of the securities acts were often independent violations of state law as well. The court wrote:

However, I think it should be made clear that some acts which constitute violations of the Securities Exchange Act and the

32. 139 A.2d 591 (Del. Ch. 1958).
33. 134 A.2d 852 (Del. Ch. 1957).
34. Id. at 865. A proxy procured to commit a fraud concealed from shareholders is of no effect. Chief Justice Southerland in Dolese Bros. Co. v. Brown, 167 A.2d 784, 788 (Del. 1960), wrote:
Defendant argues that when a meeting of stockholders has been held, and corporate action authorized by the use of general proxies permitting the exercise of unlimited discretion by the proxy holder, and that action is duly taken, the stockholder ordinarily cannot later repudiate the action of his agent. As a general proposition, this is correct [citation omitted]. But that rule has no application to a case such as this, in which the dominating director is charged with using the proxies to commit a fraud concealed from the stockholders whose vote is necessary to accomplish it, and in which no rights of third persons are affected.
The district courts of the United States . . . shall have exclusive jurisdiction of violations of this title or the rules and regulations thereunder, and of all suits in
rules and regulations formulated thereunder may also be
cognizable in a Section 31 proceeding as independent wrongs for
which this court would grant a remedy, even if the Securities
Exchange Act had never been passed.36

Somewhat later, Judge Rodney in the federal district court
recognized that evidence that would establish proxy fraud under
federal law would condemn a proxy statement in the state court.37
Any securities practitioner knows that securities fraud cases, like
most other kinds of cases, are controlled by their peculiar facts.
Thus, where we do not have the luxury of identity, comparisons
between Delaware and federal proxy cases are difficult to make.
Materiality, as it relates to misrepresentations, is a slippery concept
even in the most deft of judicial hands. Nevertheless, Delaware
courts have come to respectable grips with the concepts involved in
shareholder deception. The court in Gerlach v. Gillam, for example,
required “complete candor” and held inadequate proxy material that
by omission of “essential information” made it impossible for
stockholders to make an objective evaluation of the proposed
transaction.38

Vice Chancellor (now Chancellor) Marvel, in a tender offer case,
held that the offeror:

had a duty to exercise complete candor in its approach to the
minority stockholders of TransOcean for a tender of their

(Del. Ch. 1946), aff’d, 51 A.2d 572 (Del. 1947).
materials had previously been attacked in the Delaware Chancery Court, where they
had been cleared. Kaufman v. Shoenberg, 91 A.2d 786 (Del. Ch. 1952). The federal
court dismissed as res judicata a complaint containing the same allegations of
misrepresentation and omission as had been made in the state court. The court said:

An examination of the two complaints reveals that the same affirmative
allegations of misrepresentation and omission are included verbatim in the
present case as were made in the state court action. These allegations in both
suits are directed toward the same proxy statement which was submitted by
defendant to its stockholders in June, 1951. Clearly, the judgment sought in this
action, which is identical with that sought in the Chancery suit, is inconsistent
with the final adjudication of the Chancellor. It is also clear to me that the
evidence necessary to enable plaintiff to prevail herein would have been sufficient
to authorize a recovery by her in the state court.

154 F. Supp. at 66–67 (emphasis supplied).
24, 1977) found the standard imposed by the Court of Chancery in Lynch v. Vickers
Energy Corp., 351 A.2d 570 (Del. Ch. 1976) to be a higher standard of accountability
than that imposed under §14(e) of the Securities Exchange Act of 1934.
shares, namely a duty to make a full disclosure of all of the facts and circumstances surrounding the offer for tenders, including the consequence of acceptance and that of refusal, and insofar as the price offered is concerned that it not be one which would induce the acceptance of an unconscionable bid by an unwary stockholder at a price below the market or otherwise unreasonable under the facts and circumstances attending such offer for tenders of stock.39

Delaware courts look to the entire effect of the information presented. Specific candor will not suffice if the totality of the information tends to mislead. Conversely, isolated errors placed in the larger context may not mislead at all. Thus, in Campbell v. Loew's, Inc., the court looked not only to the accuracy of various factual representations, but also to the cumulative effect of the factual presentation to determine what "the whole impact of the proxy material conveyed to the average reader."40

III. MANAGEMENT RESPONSIBILITY

a. Fiduciary Capacity and Limitations
on the Business Judgment Rule

The Delaware statute provides: "The business and affairs of every corporation . . . shall be managed by or under the direction of a board of directors . . . who may be removed by a majority of the stockholders at any time."41

Overshadowing specific duties, a long and unchallenged line of Delaware cases makes clear that the primary duty of a director is, as a fiduciary, to deal fairly and justly with the entrusted assets in pursuit of the business objectives of the corporation. Vice Chancellor Marvel quoted the following language from an earlier case:

"It is fundamental that directors stand in a fiduciary relation to the corporation and its shareholders, and that their primary duty is to deal fairly and justly. It is a breach of this duty, wholly apart from any consideration of pre-emptive rights, for directors to make use of the issuance of shares to accomplish


40. 134 A.2d at 865; cf., In re Seminole Oil & Gas Corp., 150 A.2d 20 (Del. Ch. 1959).

41. 8 Del. C. § 141(a). Directors have numerous specific statutory powers which complement the general power. There is a specific enumeration in E. FOLK, THE DELAWARE GENERAL CORPORATION LAW, 611 app. (1972).
an improper purpose, such as to enable a particular person or group to maintain or obtain voting control, against the objection of shareholders from whom control is thereby wrested.”

Not only directors, but officers as well, are treated as fiduciaries for the benefit of the corporation, its shareholders and its creditors. The much-cited business judgment rule serves to protect the acts of both directors and officers in those cases where their expertise is greater than the court’s. Such protection only obtains, however, if the corporate officials have paid informed attention to their duties. Chancellor (now Justice) Duffy, in Kaplan v. Centex Corp., in finding a substantial judgment for the plaintiff in a derivative suit, explained this crucial limitation on the protection of the rule:

Application of the [business judgment] rule, of necessity, depends upon a showing that informed directors did, in fact, make a business judgment authorizing the transaction under review. And, as plaintiff argues, the difficulty here is that evidence does not show that this was done. There were director-committee-officer references to the realignment but none of these, singly or cumulatively, show that director judgment was brought to bear with specificity on the transactions.

Of course, the business judgment rule is wholly inapplicable if the transaction in question is not “at arms-length.”

It is said that the business judgment rule, when applicable, creates a presumption of good faith and requires a showing of bad faith or abuse of discretion to mount a successful challenge. This presumption, however, can be rebutted altogether, as in a situation of self dealing, or where the directors have passed “an unintelligent or unadvised judgment.” The rule can also lose a portion of its

47. E.g., Sinclair Oil Corp. v. Levien, 280 A.2d 717 (Del. 1971).
force if, for example, the questioned transaction was hastily executed. In a situation where full director attention is questionable, the court may scrutinize carefully the questioned transaction while still granting some quantum of weight to the presumption of sound business judgment.49

Of course, there are, other substantial limitations on corporate officers. Officers’ powers and duties arise from the corporation law, the charter, the by-laws, and board resolutions. By-laws and resolutions must not be contrary to the certificate of incorporation or a clear statutory or common law policy.50 Very little inherent authority or power in corporate officers is presumed. However, when dealing with the rights of third parties, the ordinary principles of agency and equity law frequently hold the corporation to transactions which were not, in fact, authorized in advance.51

b. Use of Insider Information

Directors who purchase their corporation’s stock from outside minority shareholders are held to the standards of a fiduciary. Delaware courts have expressly held that an insider, possessed of special knowledge of future plans or secret resources of his corporation, owes a fiduciary duty to a stockholder who is ignorant of such facts when negotiating for the purchase of his shares.52 The Fifth Circuit in Mansfield Hardware Lumber Co. v. Johnson53 simply misconstrued Delaware law when it held to the contrary.54

If a director or officer is undeterred by the prospect of damages for misrepresentation, an additional deterrent to taking advantage of inside information is found in Brophy v. Cities Service Co.55 There, an insider, privy to secret information that his corporation was planning open market purchases of its own shares, made his own purchase beforehand and then sold out at a substantial profit. The Chancellor had no difficulty holding that the director took these gains as a trustee and that the corporation was entitled to them as a

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51. FOLK, supra note 41, at 71-72.
54. Professor Cary, without analysis of Delaware law, followed the Fifth Circuit in its error. Cary, Federalism Article, supra note 1, at 663.
55. 70 A.2d 5 (Del. Ch. 1949).
constructive beneficiary. *Diamond v. Oreamuno* was hailed as a significant advance in the law when decided by the New York Court of Appeals. *Diamond* not only recognized *Brophy*’s holding but followed *Brophy* chronologically by twenty years; both stand for the same fundamental proposition:

[A] fiduciary of a corporation who trades for his own benefit on the basis of confidential information acquired through his fiduciary position breaches his duty to the corporation and may be held accountable to that corporation for any gains without regard to whether the corporation suffered damages as a result of the transaction.57

c. *Interested Director Transactions and Controlled Mergers*

Since the Delaware courts view a director as a fiduciary, it follows that he may not profit from his position of trust. When challenged, he must prove that transactions in which he has an interest are fair.

Several nationally celebrated Delaware cases serve to illustrate this proposition.

In *Keenan v. Eshleman*, the plaintiff-stockholders of Sanitary Company of America sought an accounting from three of their directors who, as principals of Consolidated Management Association, had provided “management consultation” services to Sanitary. In granting the accounting the court said of the directors: “The appellants were in absolute control of both corporations. As directors, they were trustees for the stockholders, and the utmost good faith and fair dealing was exacted of them, especially where their individual interests were concerned.”59

*Guth v. Loft, Inc.*, which condemned the usurpation of a corporate opportunity by a director, is still a leading decision on a director’s fiduciary duties:

Corporate officers and directors are not permitted to use their position of trust and confidence to further their private interests. While technically not trustees, they stand in a fiduciary relation to the corporation and its stockholders. A public policy, existing through the years, and derived from a profound knowledge of human characteristics and motives, has established a rule that demands of a corporate officer or director, peremptorily and inexorably, the most scrupulous observance of

58. 2 A.2d 904 (Del. 1938).
59. *Id.* at 908.
his duty, not only affirmatively to protect the interests of the corporation committed to his charge, but also to refrain from doing anything that would work injury to the corporation, or to deprive it of profit or advantage which his skill and ability might properly bring to it, or to enable it to make in the reasonable and lawful exercise of its powers. The rule that requires an undivided and unselfish loyalty to the corporation demands that there shall be no conflict between duty and self-interest. The occasions for the determination of honesty, good faith and loyal conduct are many and varied, and no hard and fast rule can be formulated. The standard of loyalty is measured by no fixed scale.60

More recent decisions, far from lowering the standards,61 have served to reinforce the principles found in Keenan and Guth.

Burden of proof is significant here as well. Not only are directors held to a rigid standard of conduct, but the allegation of self-dealing shifts the burden of establishing the entire fairness of the challenged transaction to the defendant director. In Keenan, upon noting that the defendants were on both sides of the transaction which resulted in their being paid handsome consulting fees, the court declared: "[D]ealing as they did with another corporation of which they were sole directors and officers, they assumed the burden of showing the entire fairness of the transaction."62

A similar expression of the rule appears in Johnston v. Greene,63 a case that involved the offer of various patents to a corporation by its dominating director: "The refusal of the directors of Airfleets to buy the patents was, under the Chancellor's finding, a transaction between the dominating director and his corporation. It is therefore subject to strict scrutiny, and the defendants have the burden of showing that it was fair."64

The ultimate standard which the interested director must satisfy is succinctly stated in Johnston. If the court can be satisfied that a "wholly independent board of directors" would have reached the same decision on the transaction, given the information supplied by

60. 5 A.2d 503, 510 (Del. 1939).
62. 2 A.2d at 908.
63. 121 A.2d at 925; see also Gottlieb v. Heyden Chemical Corp., 90 A.2d 660 (Del. 1952).
the interested director, then the transaction is deemed fair and will be upheld.65

Delaware applies the same shifting burden where, in a merger or other reorganization, one of the constituent corporations is on both sides of the transaction.66 Some of these most recent and colorful cases have been popularly termed "going private."67

d. Reclassification of Shares

Reclassification of shares is an essential tool of capital flexibility. Although abuses can occur through improper use of this device, Delaware law forbids such impropriety.68 Where a reclassification is effected by means of direct charter amendment,69 the holders of the outstanding shares of any class are entitled to a class vote if the amendment increases or decreases the aggregate number; increases or decreases the par value; or alters or changes the powers, preferences or special rights of their shares so as to have an adverse effect. For example, the direct elimination of dividend accruals is now permitted by charter amendment.70 If the amendment would eliminate the accrued preferred dividends, the majority of the preferred shareholders, as a separate class, must approve the proposal.

A further protection is provided by the inherent power of the Court of Chancery to enjoin or rescind a reclassification if it is unfair to a segment of stockholders. Topkis v. Delaware Hardware Co. held: "[A] power conferred by statute upon a majority of the stockholders or upon directors, though conferred in terms that are absolute, is nevertheless subject to restraint by a court of equity if it be inequitably exercised."71

65. 121 A.2d at 925.
67. Cf. two recent going private cases decided by Vice Chancellor Marvel: Pa. Mutual Fund, Inc. v. Toshunter Int'l, Inc., No. 4845 (Del. Ch. Aug. 5, 1975), reprinted in 1 DEL. J. CORP. L. 229 (1976) (merger restrained because "use of control to freeze out or to manipulate a corporation to the detriment of minority stockholders has always been frowned on by this court"); Lynch v. Vickers Energy Corp., 351 A.2d 570 (Del. Ch. 1976) (the court, after a trial on the merits, found adequacy of disclosure and price and rejected a challenge to an allegedly "coercive" tender offer by the majority.)
68. Cary, Federalism Article, supra note 1, at 677, 678, maintains that reclassifications and similar reorganizations are examples of how the Delaware courts will permit one class of shareholders to profit at the expense of another class. His criticism ignores the statutory and case law.
69. 8 DEL. C. § 242.
71. 2 A.2d 114, 119 (Del. Ch. 1938).
Proof of constructive fraud will condemn a recapitalization plan as unfair. 72 Constructive fraud has been defined as (1) "acts of bad faith, or a reckless indifference to the rights of others interested, rather than from an honest error of judgment" 73 or (2) "improper motive or personal gain or arbitrary action or conscious disregard of the interests of the corporation and the rights of its stockholders." 74

e. Appraisal Rights

Reclassification, of course, can be accomplished by a merger or consolidation. Mergers, like charter amendments, are subject to safeguards which protect the interests of minority shareholders.

Where there is a thin market, a stockholder dissenting from a merger has a right to an appraisal of his stock. 75 The stockholder must object in writing to the merger and demand payment for the value of his shares. If he and the surviving corporation do not agree, he or the corporation may begin an appraisal proceeding.

The Delaware courts have identified various factors which are to be considered and weighed in arriving at a valuation for stock in an appraisal proceeding: "[T]he actual or true value of the stock is to be determined by considering the various factors of value including earnings, dividends, market price, assets, and the other factors deemed relevant in a stock evaluation problem arising under the Delaware Corporation Merger Statute, 8 Del. C. § 262." 76 Furthermore, the over-riding consideration is that all factors relevant to a determination of fair price in a particular situation are to be examined and weighed as appropriate to the circumstances of the particular corporation and merger. The courts recognize that the determination of fair price necessitates much balancing and judgment.

Thus, for example, in Sterling v. Mayflower Hotel Corp., 77 the Supreme Court accorded less weight to net asset value than market value:

But the requirement that consideration be given to all relevant factors entering into the determination of value does not mean that any one factor is in every case important or that it must be

75. 8 Del. C. § 262.
76. Poole v. N.V. Deli Maatschappij, 243 A.2d 67, 69 (Del. 1968). These factors are customarily grouped under the three principal headings of market value, earnings value and net asset value.
77. 93 A.2d 107 (Del. 1952).
given a definite weight in the evaluation. . . . The relative importance of several tests of value depends on the circumstances. Thus, in some cases net asset value may be quite important. . . . But in the case at bar it is of much less importance than the factors analysed in the [investment banker's] report. We are dealing here with corporations engaged in the hotel business, whose capital is invested largely in fixed assets. The shares of such corporations are worth, from the viewpoint of an investor, what they can earn and pay. A comparison of net asset values may have some weight, but it is of much less importance than demonstrated capacity of the corporation to earn money and pay dividends.\(^78\)

In appraisal proceedings, as elsewhere, the courts of Delaware look to the circumstances of the particular case in applying statutory and common law as the equities require.

Much of the recent criticism of appraisal had to do with its complexity and cost.\(^79\) Two recent developments show that such criticism is baseless or outdated. The Delaware Supreme Court in *Raab v. Villager Industries, Inc.*\(^{50}\) recently reaffirmed that: "The requirements of §262(b) are to be liberally construed for the protection of objecting stockholders, within the boundaries of orderly corporate procedure and the purpose of the requirement."\(^81\) Perhaps more importantly Chief Justice Herrmann on that occasion announced a prospective policy. Before proceeding with a merger, the Chief Justice said, Delaware corporations must make sure that their stockholders are fully informed of their rights under section 262:

A Delaware corporation, engaged in §262 proceedings, henceforth shall have an obligation to issue specific instructions to its stockholders as to the correct manner of executing and filing a valid objection or demand for payment under the Statute, as construed by Delaware courts, including: (1) the general rule that all such papers should be executed by or for the stockholder of record, fully and correctly, as named in the notice

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80. 355 A.2d 888 (Del. 1976).

81. Id. at 891 (emphasis supplied). *See also* Salt Dome Oil Corp. v. Schenck, 41 A.2d 583 (Del. 1945); Carl M. Loeb, Rhoades & Co. v. Hilton Hotels Corp., 222 A.2d 789 (Del. 1966); and Raynor v. LTV Aerospace Corp., 331 A.2d 393 (Del. Ch. 1975).
to the stockholder; and (2) the manner in which one may purport to act for a stockholder of record, such as a joint owner, a partnership, a corporation, a trustee, or a guardian.

Fairness to stockholders requires such reasonably specific instructions in §262 proceedings. As a general rule in the future, failure by the corporation to furnish such instructions will result in the resolution in favor of the stockholder of all doubt as to the sufficiency, for corporate purposes, of the objection or demand.82

Further, effective July 1, 1976, the General Corporation Law was amended by the Delaware General Assembly to permit reimbursement of attorney's fees and simplification of appraisal procedures. The official commentary sets out the purposes sought to be attained:

The present statute contains circuitous and arbitrary provisions governing the time limits for an appraisal so that an appraisal action may be filed up to four months and 50 days following the effective date of the merger. Under the proposal to §262(c), this period would be changed to 120 days and provisions made for the filing of an appraisal action immediately following the effective date of the merger. However, the stockholder has been afforded the opportunity to change his mind and withdraw the appraisal action during the first 60 days of the 120 day period.

... .

The proposed revisions to §262(b) are intended to provide a more equitable means of sharing the cost of an appraisal. Under the present practice, each stockholder bears his own expenses in the appraisal so that if one stockholder hires an attorney and expert witnesses, he must bear all of the expenses while all of the other stockholders receive the benefit of the attorney's representation and the testimony of the expert witnesses. This has resulted in unfairness to the stockholder who has neither the money nor a sufficient stock interest in the corporation to hire attorneys and experts. Also, the stockholder who does hire attorneys and experts is unfairly taxed with all of the cost. Under the proposed revisions of §262(h), all of the stockholders would share the expenses of the attorneys and experts who have achieved a benefit for them.83

There are, of course, well-recognized circumstances under which a stockholder need not choose between appraisal and accepting the

82. 355 A.2d at 895.
merger. Where unfairness amounts to fraud, actual or constructive, the stockholder may enjoin the merger. If a constituent corporation is “on both sides” of the transaction, the burden of proving the intrinsic fairness of the transaction, under the careful scrutiny of the court, is wisely shifted to the defendant corporation.

f. Indemnification

Many commentators have viewed with alarm the greatly increasing risk, potential liability, and involvement in litigation which arises from serving as a corporate director. The need for qualified management is axiomatic. Increasingly, there has been a call for the presence of outside directors to provide corporations with skillful independent advice and to represent points of view potentially different from that of internal management. The 1967 amendment to the Delaware indemnity provision represented an effort, considering these factors, to enable corporations to provide adequate protection to such officers and directors for expenses that might arise in defending themselves.

The Delaware solution struck a responsive chord. In an example that is the sincerest form of flattery, the 1967 Delaware amendment was adopted verbatim by the Committee on Corporate Law of the American Bar Association for inclusion in the Model Act. It is now the law in twenty-six states. Delaware’s section 145 has only been amended to include in its scope officials of predecessor entities and has, since its adoption, been applied countless times to protect directors and officers from unjustified expense. Very little

84. As an additional problem with reclassifications, Professor Cary has said that the Delaware courts have avoided looking through form to substance, Federalism Article, supra note 1, at 677. In support of this he cited, alternatively, Keller v. Wilson & Co., 190 A. 115 (Del. 1936) and Federal United Corp. v. Havender, 11 A.2d 331 (Del. 1940). Since 8 Del. C. § 242(a)(4) now permits elimination of dividend accruals by charter amendment, Cary is wrestling with a dead issue.


87. See McAdams, A Proposal to Amend the Indemnification Section (§ 5) of the Model Business Corporation Act, 31 Bus. Law. 2124 (1976); Brook, Directors’ Indemnification and Liability Insurance, 21 N.Y.L.F. 1 (1975); Greenberg & Dean, Protecting the Corporate Executive: Director And Officer Liability Insurance Reevaluated, 58 Marq. L. Rev. 555 (1975).


89. 8 Del. C. § 145.

90. ABA-ALI MODEL BUS. CORP. ACT § 5 (1956).

litigation has resulted. Critics of section 145 have centered on two areas.

Some have raised questions as to mandatory indemnification for expenses in instances where the litigation against the corporate official terminates for technical reasons or, in a criminal case, on a plea of nolo contendere. Such critics doubt that the second Wolfson case is correctly decided because Wolfson had been convicted on a related count. Others believe that section 145 should be amended to permit indemnity in such cases only for the director who proves his lack of culpability. These may be valid issues. Nevertheless, significant in this area is the pioneering and progressive role Delaware has played in dealing promptly and thoroughly with the question at — and before — the time the issue became critical.

The indemnification provisions have also been criticized for allowing corporations to pay insurance premiums for directors’ and officers’ liability insurance policies. This analysis is faulty.

No responsible insurer will make coverage available to protect directors against liability for defalcations or breaches of trust. Even a tentative inquiry into the subject of available coverage makes this plain. As do lawyers’ and doctors’ malpractice insurance plans, director and officer liability insurance serves both to protect the insured against consequences of negligence, and to benefit the victims of that behavior by providing a compensation fund.

IV. Competition for Control

a. Available Tools

When an outsider or a group of stockholders seek to replace incumbent management, the structure of the corporation law receives a severe test. Perhaps it is in the corporation’s best interest for the outsiders to succeed. As Professor Cary has written: “The raider may sometimes be a better manager than the ‘raidee.’”

However, as the word “sometimes” would suggest, the matter is not black and white. “Raiders” and others frequently use surprise


93. 8 Del. C. §§145(f), 145(g); Cary, Federalism Article, supra note 1, at 669–70; but see Greenberg & Dean, supra note 87, at 575.

94. Cary, Federalism Article, supra note 1, at 675.
tactics and market forces, such as stampede and arbitrage; foul play is not unknown. Financing for a takeover may make real or thinly veiled use of the target's own credit. Certain stockholders of well-managed and conservatively financed businesses may be offered a quick profit to the disadvantage of other stockholders at a time of depressed market price. A good corporation law must deal in the context of its more permanent structure, with the abuses on all sides that arise in competitions for control, and must strike a fair balance between the competing considerations.

In order to perform their duties properly in the face of a raid or attack believed contrary to the interests of the stockholders, the directors must have available to them as many legitimate tools as possible to defend those interests. The field is well developed. Capital structure may be flexible, with power to buy or sell securities — whether common stock, preferred stock, convertible securities or warrants — together with the statutory and charter authorization to use them. To act promptly, a large board must be able to delegate decision-making to a smaller committee of its members.

Continuity of board membership can provide the stability that is particularly, but not exclusively, desirable when a company is engaged in a financial recovery or undergoing otherwise difficult times. Such a board prevents the wholesale replacement of all the knowledgeable members. Prohibition, in certain cases, of the removal without cause of board members by shareholders is as important an adjunct to the procedure as the ability to effect that removal may be in other circumstances. Mergers and other major corporate changes for many years required votes of substantially more than 51% of the stockholders. Normal business flexibility may require the lower majority vote, which is the general rule. Nevertheless, a higher vote, if adopted by the stockholders, may retard or inhibit takeover.

A corporation whose shares are selling at a depressed price may desperately need, but not attract, the best managers because of the

96. 8 Del. C. §§122(4), 123, 160.
97. 8 Del. C. §141(c); but see Folk, Corporation Law Developments—1969, 56 Va. L. Rev. 755, 790 (1970).
101. 8 Del. C. §§102(4), 242(c)(4).
hazards of short tenure. These hazards may also require the payment of undesirably high salaries. What the shareholders of such a corporation do not need is corporate war, but rather a corporate peace in which to develop or recover resources. In such cases, management's needs may not be "entrenchment" so much as "peace of mind." If such is the will of the stockholders, a proper statute should make the tools available; and the Delaware statute does.

On the other hand, the available tools are subject to abuse. Delaware courts have time and again condemned and proscribed such abuse. It was a corporate takeover fight that gave rise to that touchstone of Delaware corporate common law: "[I]nequitable action does not become permissible simply because legally possible." 102

Experience has shown that, by merger with another company, or through a competing offer, a target can often obtain, for its stockholders a higher price or price equivalent per share than the first offeror is willing to provide. To make the alternative transaction in the face of a raid, management needs capital flexibility and time to act.

A potential target must have sufficient securities available to provide for splits in common or issuance of securities in connection with acquisitions. The statute provides for the initial capitalization 103 and permits amendment of the certificate of incorporation to increase or reclassify authorized common stock. 104 Preferred may be authorized subject to the board's authority to fix the rights and preferences without amendment of the charter. 105 Convertible securities may be created for later use. 106 This is not to say that the manipulation of shares to perpetuate management is encouraged. Only a failure to read the Delaware cases would lead to such a conclusion.

b. Abuse of Capital Flexibility

i. Sale of stock to insiders and increasing authorized shares

Delaware courts have long applied strict fiduciary rules to the purchase and disposition by the corporation of its own securities. More than a half century ago, Chancellor Josiah O. Wolcott wrote:

Directors of a corporation are frequently spoken of as its trustees. Their acts are scanned in the light of those principles

103. 8 Del. C. § 102(a)(4).
104. 8 Del. C. § 242(a)(3).
105. 8 Del. C. §§ 102(a)(3), 151(a), 242(a).
106. 8 Del. C. §§ 151(a), 242(a)(5).
which define the relationships existing between trustee and cestui que trust. Tested by these familiar principles, [that] the three directors who thus conspired to take from the company enough stock to fix themselves in undisputed control of its affairs, is reprehensible. 107

As recently as last year, Vice Chancellor Marvel enjoined a corporation from increasing its authorized shares to eliminate a 50% stockholder from his position. 108 The basis for this ruling is time honored fiduciary principles governing the relationship between directors and stockholders.

Many Delaware cases have declared that efforts to “freeze out” a minority interest are actionable without regard to the fairness of price, 109 and, similarly, an effort to eliminate majority voting control by the issuance of stock without first offering the majority holder the right to buy has been enjoined. 110

In Condec v. Lunkenheimer, Vice Chancellor Marvel stated these principles flatly: “[S]hares may not be issued for an improper purpose such as a takeover of voting control from others. . . . The converse of the above rule is also established, namely that corporate machinery may not be manipulated so as to injure minority stockholders.” 111

In Condec, the target company (Lunkenheimer), fighting off a takeover, had sought to increase the float of common stock to abort an apparently successful tender offer by “purchasing” an asset from the merger partner whom management wished to “marry.” This, the court wrote, “is a case of a stockholder [the offeror] with a contractual right to assert voting control being deprived of such control by what is virtually a corporate legerdemain. Manipulation of this type is not permissible.” 112

111. 230 A.2d 769, 775 (Del. Ch. 1967).
112. Id. at 777. The Vice Chancellor said: If it is a breach of . . . [fiduciary] duty, wholly apart from any consideration of preemptive rights, for directors to make use of the issuance of shares to accomplish an improper purpose, such as to enable a particular person or group to maintain or obtain voting control, against the objection of shareholders from whom control is thereby wrested.

Id. at 775, quoting Yasik v. Wachtel, 17 A.2d 309 (Del. Ch. 1941).
ii. Purchase and redemption of shares

Recently, on similar principles, Vice Chancellor Brown dealt with the use of corporate funds by management, not to issue more shares, but to selectively redeem certain shares of voting stock held by a member of management in a voting trust.\textsuperscript{113} The voting trustee and his associates on the board had voting control of the corporation without the use of the trust shares and the trust was to expire in about six months. Upon the expiration of the trust, control would effectively shift away from the trustee and his associates in management and devolve on the beneficial owners of the trustee shares. To make matters worse, the redemption was selective; that is, the remaining preferred stock, all of which was held outright by the trustee and another director, was not scheduled for redemption. The Vice Chancellor restrained the redemption:

In addition, it is unquestionably Delaware law that the use of corporate funds to purchase corporate shares primarily to maintain management in control is improper. [Citations omitted.] Here it appears that redemption of all preferred shares other than those owned by Leslie and Nadeau will assure their continued control of Penntech (even though they may not be under open assault at present) and particularly if it does away with such shares prior to the expiration of the voting trust which present management now controls. Under such circumstances, a selective redemption of a large amount of voting stock which thereby guarantees control in those determining to make the redemption would initially seem no different in result than a purchase of shares with corporate funds to remove a threat to incumbent management policy and control, in which letter case the burden is on the directors to justify the purchase as one primarily in the corporate interest and not their own [citation omitted.]

At this juncture, to redeem all other preferred stock, but none of their own, so as to continue their own business incentive and to avoid a possible, but yet unsubstantiated, tax consequence to the other preferred shareholders, does not appear sufficient to carry the day for the present defendants when the various other factors alleged by the plaintiff are considered.\textsuperscript{114}

The Petty court cited Bennett v. Propp as controlling.\textsuperscript{115} In Bennett, the target corporation bought its own shares in an effort to

\textsuperscript{114} Id. at 143.
\textsuperscript{115} 187 A.2d 405 (Del. 1962).
thwart a tender offer. The Delaware Supreme Court had affirmed a derivative plaintiff’s judgment on behalf of the corporation against two of the directly responsible officers and directors. The Supreme Court stated the proposition in clear terms: “Sadacca’s purchases were made to preserve the control of the corporation in himself and his fellow directors. . . . The use of corporate funds for such a purchase is improper.”

A management that seeks to abuse the capital flexibility made available by the statute and manipulate its capital, or indeed perform any act in order to stay in office, in the face of the overwhelming authority in the Delaware courts, not only runs a grave risk of having its actions restrained or annulled, but also of paying dearly for the effort.

c. Granting Time to Stockholders and Management

Many state legislatures have felt that the timing set out in the Williams Act, which permits a tender offer to be made and closed over a ten day period, did not give management time to exercise its fiduciary duty, the stockholders time to consider the worth of the offer, or competitors time to raise the price.

Between 1968 and mid-June 1976, nineteen states enacted laws to deal with the problem. It was widely recognized as a legitimate legislative goal to protect a target’s stockholders by giving them sufficient time and information to make a considered and knowledgeable decision. However, it has been charged that one of the major purposes of such statutes is to protect entrenched management. The mechanism for such abuse lies in the fairness hearing to be held by the state’s securities commissioner. Such hearings are frequently protracted and, in most cases, occur before a politically appointed officer who has no love for the out of state offeror. In April 1976,

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116. In the trial court, the Bennett case had been decided by the same Vice Chancellor who had two years before decided Kors v. Carey, 158 A.2d 136 (Del. Ch. 1960). The Kors case had recognized an exception to the rule, recited also in Cheff v. Mathes, 199 A.2d 548 (Del. 1964), in cases where directors reasonably believe that the takeover would be injurious to the company.

117. 187 A.2d at 408.

118. Sections 13(d), (e) and 14(d), (e) and (f) of the Securities Exchange Act of 1934, 15 U.S.C. §§ 78m(d)–(e), 78(d)–(f) (1970).


120. At the time Delaware enacted its law, such provisions for hearing existed in Hawaii, Idaho, Indiana, Kansas, Minnesota, Ohio, Pennsylvania, South Dakota, Virginia, and Wisconsin; prior to 1976, only Colorado and Nevada did not provide for such a hearing.
after careful study, Delaware adopted such a law as new section 203 of the General Corporation Law. The official comment accompanying the bill outlines its basic terms and aims:

During the past several years a number of public offers to purchase shares of stock in a corporation have been made upon such short notice that the shareholders have not been given ample opportunity to determine if the offer is fair, or to see if some more favorable offer might be made in the auction of an open market. Even management in some instances has not had time to evaluate the fairness of the offer and to determine whether to recommend it to its shareholders, to oppose it, or to take no position. The statute here proposed would require any such offeror to give notice to the corporation of the basic terms of a proposed offer 20 days before it is to open and to keep the offer open for a minimum of 20 days. By providing this minimum period of 40 days, the shareholders will have time to evaluate the offer, and the marketplace will have an opportunity to react to the offer.122

Thus, Delaware neither permits the “saturday night special,”123 which favors the underpriced raid, nor does Delaware go to the other extreme and grant management a friendly forum in which to avoid a fair competitive offer for the stockholders’ shares.

V. Remedies

Delaware offers corporations and stockholders a specialized forum and procedures for the prompt enforcement of their rights. Article IV of the Delaware Constitution of 1897, and chapter 3 of title 10 of the Delaware Code, establish the Delaware Court of Chancery as the separate equity court, with jurisdiction to oversee operations of Delaware corporations and to enforce the General

121. 8 Del. C. §203, effective May 1, 1976. Section 203 received its first appellate review in Monogram Indus., Inc. v. Royal Indus., Inc., 367 A.2d 650 (Del. 1976), opinion rendered, 372 A.2d 171 (Del. 1976), rev'g, 366 A.2d 839 (Del. Ch. 1976). In that case the court, per Herrmann, C.J., reversed the Court of Chancery and rejected a “hypertechnical” position based “more upon target-company defense tactics than sound principles of statutory construction.”


123. “Among attorneys the shortest offers are drawing the most fire. Despite some recent successes, pressure is building for change. Called Saturday Night Specials, quickies or blitzkriegs, these offers run no more than eleven days — including weekends — and are designed to take the hostile target by surprise, panic the shareholders into selling, and just barely meet the Williams Act’s seven-day minimum time period.” J. FITZHUGH, CASH TENDER OFFERS: RAGE AND OUTHAGE, at 165 (1976).
Corporation Law. The court's work gives its judges the experience necessary for informed application of equitable and corporate law principles.

The men who have served as chancellors and vice chancellors have had, almost uniformly, distinguished records of public service. The judges' decisions, cited and quoted above, show their enlightened concern for intra-corporate justice.

Delaware law provides a number of situations in which the Court of Chancery is specifically empowered to take particular steps to protect stockholder interests. Some of these situations have been discussed previously. Other examples of similar significance can be cited. Considered together, however, these statutory remedies are only a part of those available to litigant stockholders.

A stockholder can bring suit in Chancery to enforce an individual, class or derivative claim arising under the corporation law. Such suits may seek money damages, or preliminary and permanent injunctive relief, as well as specific performance of

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124. Professor Cary attacked Delaware judges generally in an unfortunate ad hominem passage. Cary, Federalism Article, supra note 1, at 690–96. The cases cited in the earliest portion of this review seem to us a better defense to Cary's charges than engaging in the same notoriously dangerous "social jurisprudence;" that is, trying to predict a judge's vote from his personal history. Cary's "history" itself is wrong. Many Delaware judges come from the rural part of the State, e.g., Justice McNeilly and Vice Chancellors Brown and Hartnett. The rest have risen primarily through extensive service on the courts, not private practice, e.g., Chief Justice Herrmann, Justice Duffy and Chancellor Marvel.

125. 8 Del. C. § 211 (Meetings of Stockholders); see also Del. Ch. Ct. R. 81, which sets out the procedures for a corporate election held by court order and allows punishment of recalcitrant directors for contempt of court; 8 Del. C. § 220 (Stockholder's Right of Inspection); 8 Del. C. § 225 (Contested Election of Directors: Proceedings to Determine Validity); 8 Del. C. § 262 (Payment for Stock or Membership of Person Objecting to Merger or Consolidation).

126. E.g., 8 Del. C. § 168 (Judicial Proceedings to Compel Issuance of New Certificate); 8 Del. C. § 223 (Vacancies and Newly Created Directorships); 8 Del. C. § 226 (Appointment of Custodian or Receiver of Corporation on Deadlock or for Other Cause); see also Del. Ch. Ct. R. 160; 8 Del. C. § 278 (Continuation of Corporation After Dissolution for Purposes of Suit and Winding Up Affairs); 8 Del. C. § 183 (Revocation or Forfeiture of Charter Proceedings).


129. E.g., Brophy v. Cities Service Co., 70 A.2d 5 (Del. Ch. 1949) (derivative action to require corporate employee to account to the corporation for profits realized from insider trading).

130. E.g., Gimbel v. Signal Cos., Inc., 316 A.2d 599 (Del. Ch. 1974) (class action by minority stockholder to enjoin sale of stock in wholly owned subsidiary).
statutory or contractual obligations or such other relief as the court finds appropriate. Whatever the relief sought, stockholders' suits receive prompt attention from a judge whose docket is not overly cluttered.

Moreover, Delaware has adopted a director service statute, 10 Del. C. §3114, which permits service of process on nonresident directors of Delaware corporations when the matter in litigation arises out of an alleged violation of the director's duty to his corporation or its stockholders. Thus, Delaware affords "a convenient and available forum for supervising the affairs of Delaware corporations and the conduct of directors of Delaware corporations."

However, the existence of judicial stockholder litigation machinery does not necessarily assure the protection of minority rights. Rules can be burdensome or expensive. Delaware, unlike some states, does not discourage stockholder litigation by requiring a substantial bond for costs. The rules with respect to pleading and prosecuting class and derivative actions are modeled after the federal rules for maintaining such actions and contain no unusual inhibitions or restrictions. With respect to the requirement that a derivative plaintiff make a prior demand upon the board or fellow shareholders to bring suit, the Delaware rule is so liberal as to make that requirement a virtual nullity.

Compromise or dismissal of stockholder derivative or class litigation is rigidly controlled by the court in order to insure that the


133. Unlike most state and federal courts, the Delaware Court of Chancery remains strictly a court of equity. 10 Del. C. §341. Delaware's "law" court, the Superior Court, is charged with jurisdiction over such burgeoning areas of litigation as criminal, tort and domestic relations cases. 10 Del. C. §541. This makes the Court of Chancery expert in the traditional areas of equity such as trusts, estates and fiduciary relations, as well as the corporation law.

134. The purpose and intent of this legislation is to fill a void in enforcement and interpretation of Delaware corporation laws created by the decision of the United States Supreme Court on June 24, 1977 in Shaffer v. Heitner, [45 U.S.L.W. 4849]. In that case, the Court struck down 10 Del. C. §366 which until now has frequently been the only means whereby nonresident corporate directors of Delaware Corporations could be brought before the courts of this State to answer for their conduct in managing the affairs of the corporation. Official Commentary to 10 Del. C. §3114, enacted July 7, 1977, to become effective September 1, 1977.

nonparticipating minority is protected. Notice provisions are, if anything, more rigorous than under the federal rules.

The court's role in passing upon proposed compromise of stockholder actions has always been more than cursory. Where an objection is made, the objecting stockholder or class member has a right to reasonable discovery and may conduct an evidentiary hearing with respect to the fairness of the settlement. Proposed settlements in stockholder litigation have been disallowed because of inadequate protection of corporate or minority interests.\textsuperscript{136} Even where the objection has been denied, the proceeding or review has resulted in an improvement of the deal for the benefit of minority shareholders. \textit{Manacher v. Reynolds},\textsuperscript{137} for example, an appeal to the Delaware Supreme Court from a Chancery decision that a settlement was fair, was compromised by substantial improvement in the terms of the settlement.

Nor has the Court of Chancery been reluctant to award substantial counsel fees, where plaintiffs have been successful in achieving meaningful benefits for the minority shareholders or the corporation by judgment or by compromise. Such awards provide real incentive to minority shareholders and their attorneys to challenge questionable corporate transactions.\textsuperscript{138}

Stockholders do, in fact, take advantage of such remedies. In 1973 through 1975, 897 actions were filed with the court in New Castle County. Of those, close to one-third (258) dealt with corporate matters; 63 of which were filed derivatively. Furthermore, 73 sequestration orders were entered by the court to compel appearances by nonresident defendants. In corporate and other matters, Chancery issued 90 orders granting interlocutory injunctive relief.\textsuperscript{139}

\begin{footnotes}

\item 137. 165 A.2d 741 (Del. Ch. 1960).

\item 138. Those who may conclude that, on some statistical basis, the rulings of the Delaware courts more often favor management than complaining stockholders overlook the fact that defendant management is likely to take to final judgment only those cases in which they believe their position to be strong. Cases in which the exposure to liability is great, or even slightly more than marginal, are frequently resolved by compromise, which results are generally never reflected in reported decisions.

\item 139. These figures and others reflecting the court's docket are informally maintained pursuant to direction of the Chancellor by the law clerks of the Court of Chancery.
\end{footnotes}
VI. CONCLUSION

We have sought to set out certain substantial principles underlying Delaware Corporation Law, as well as the procedures available for their enforcement. We will have achieved our purpose if the result is a greater understanding in the reader of these significant features of the law, and an understanding of the courts' concern for a fair balancing of the interests of all parties to corporate disputes.