DELAWARE, THE FEDS, AND THE STOCK EXCHANGE:
CHALLENGES TO THE FIRST STATE
AS FIRST IN CORPORATE LAW

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ABSTRACT

Delaware faces an unprecedented challenge to its role as the dominant law-giver as to corporate law. Its reign is not imperiled by the other states racing with Delaware but by the federal government and the stock exchanges. These alternative law-givers have long accorded state law a broad berth to define the relative rights of shareholders, directors, and officers within a corporation. In the aftermath of the Enron scandals, Delaware adopted more of a status quo response while the other two law-givers added additional obligations that intrude into the space long occupied by Delaware. This article identifies the core parts of what might be called Delaware's mission statement as to corporate law: trust directors, let them decide how they want to use the various gatekeepers, contracts, and market constraints (including not using them if they see fit) with occasional judicial check via fiduciary duty cases. The post-Enron federal and stock exchange rules seek to narrow the discretion that directors have to act by, for example, imposing new obligations directly on officers and regulating duty of care type concerns that traditionally have been the province of state law. The article concludes with suggestions of how Delaware might adapt its law given its mission statement and the current realities of the other law-givers to shore up its dominant position in making corporate law.

I. INTRODUCTION

Delaware is at the center of corporate law in America. That centrality, however, increasingly is being challenged by the federal government's redefinition of securities law to include more of corporate governance. The stock exchanges have encroached further on Delaware's space through the expansion of their listing standards that relate to internal corporate governance. While Delaware courts have recently become more aggressive in defining the role of independent directors, the dominant

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Delaware response has been more status quo oriented in addressing this growing alternative regulation of corporate governance.

This article addresses the current challenges to Delaware's primacy and evaluates possible responses. Part I begins with a brief effort to define what might be called Delaware's mission statement as to corporate law. Given Delaware's approach as reflected in this suggested mission statement, the article then explores how this position affects corporate governance issues addressed in Delaware and those issues addressed elsewhere. This initial discussion provides a baseline to evaluate Delaware's position in the wake of Enron and other recent corporate scandals. The conclusion proposes several substantive changes that Delaware should consider.

II. DELAWARE'S MISSION STATEMENT AS TO CORPORATE LAW

A mission statement is a useful beginning point for a discussion of how Delaware should respond to the current challenges to its primacy. Although such statements are now a common part of many collective institutions in our society, they are not explicitly part of something as broad and multifaceted as corporate law. I believe, however, that Delaware law implicitly reflects a recognizable mission statement that, if set out in writing, will facilitate the discussion of the state's current role vis-à-vis the federal government and the stock exchanges.¹

My suggested mission statement has four parts, expressed below with a brief explanation.

One, to establish the essential legal framework that permits the creation of corporations as real persons separate from those who own and act for them; to create the three key players in corporate governance—directors, officers and shareholders; and to define the space within which each of these groups interact in making corporate decisions. Creation is the most powerful role that corporate law fills. Government permits private planners to create artificial legal persons distinct and independent from those who own and manage the entity. The authority to create artificial legal persons is the most dramatic impact that corporate law has on our economy and society. Creation remains a state law function; the federal government creates only a small number of the corporations that

¹Any outsider, particularly one resident from a distant state, should tread lightly in volunteering for such a task. Yet Delaware corporate law has a rich history of giving room to self-appointed champions to raise corporate governance issues, such as derivative suits where one shareholder, and an attorney representing that shareholder, is able to bring suit on behalf of the corporation.
exist in the United States today, and the stock exchanges do not address creation issues at all.²

This creation authority shapes internal corporate governance beginning with the corporate actors authorized by state law. The corporations code of Delaware and the other states name only three sets of actors that are relevant to corporate governance: directors, shareholders, and officers. There are, of course, other stakeholders—employees, creditors, suppliers, and the community, who play a key part in the enterprise; many commentators want these groups to have roles in corporate governance.³ The fact that these groups are not mentioned in the corporations statute, however, is very relevant to the space that Delaware wants corporate law to occupy and what it leaves to other law.⁴

Two, to provide a straightforward, predictable governance structure whose central tenet is to trust directors. Among the three groups identified in the corporate statute, state law focuses predominantly on only one—the directors. Director centrality is the Rule #1 in understanding Delaware law. It is, of course, the express message of Section 141 and the touchstone principle of many Delaware cases.⁵ Shareholders are given a limited ability to check the broad grant of power to directors, but only in carefully measured doses. Shareholders can do three things—vote, sell, and sue—and each is very limited under Delaware law.⁶ Comparatively, the statute's role for the third set of actors, officers, is almost nonexistent.⁷ The

²Separateness issues, such as piercing the corporate veil, arise more often today under federal law than in earlier times, but this core question is still primarily a state law issue. Robert B. Thompson, Piercing the Corporate Veil: An Empirical Study, 76 CORNELL L. REV. 1036, 1049 tbl. 3 (1991) (finding 647 of 1585 piercing the veil cases arose under federal law).

³Employees, for example, are a key part of corporate statutes in other countries such as Germany where there is a supervisory board on which labor has half of the seats. They are not mentioned in Delaware’s structure.

⁴See Mark Roe, Delaware’s Politics (working paper) (describing space within which Delaware acts are dominated by managers and space where Congress’ acts which are more likely to include other groups). See also Mark J. Roe, Takeover Politics in THE DEAL DECADE 334 (Margaret M. Blair ed. 1993) (arguing changes in Delaware takeover law partially explicable by the gravitational pull of federal law.)

⁵See, e.g., DEL. CODE ANN. tit. 8, § 141(a) (2001) (stating that all corporate power is to be exercised "by or under the direction of a board of directors").


⁷Delaware Code § 142 refers to officers but the statute defers almost completely to the bylaws or board resolutions as to what they might do, how they are chosen and how vacancies are filled, except for minimal default provisions such as saying that officers may resign at any time. DEL. CODE ANN. tit. 8, § 142 (2001). The next section of the statute addresses loans to employees and officers. Id. § 143. Section 145 includes officers along with directors and others as person whom the corporation may indemnify. Id. § 145. The Model Business Corporation Act goes further and includes a section setting standards of conduct for officers. See MODEL BUS. CORP.
law designates officers as agents of the corporation and directors may give the officers however much authority and responsibility as the directors might wish.  

Three, to permit the law's governance framework to take advantage of the rich array of constraints beyond law. This principle, unlike the first two, is not directly stated in the statute, but it is as important to understanding the mission statement as either of the principles expressly set out in the statute. Corporate law is modest. The law does not expect to carry the entire burden of specifying corporate governance, particularly if this process can be done elsewhere in a less expensive manner. A variety of constraints may limit director power including: (a) markets such as those for products, capital, executive employment, and corporate control; (b) incentives and monitoring provided by specific private ordering such as executive compensation contracts and widespread use of auditors and other monitoring agencies including independent directors; and (c) norms, which play a crucial part in defining corporate governance in statements like those of the Business Roundtable, the Conference Board, or other assertions of business and community ethics. The genius of Delaware corporate law is the flexibility it permits directors to use any or all of those constraints in whatever combination that proves effective. Directors may pick from the menu of constraints in order to adjust to any new challenges as they may arise.  

Four, to provide a means to bring "our law current" on an ongoing basis, occasionally through statutory changes, and more regularly through
the gap-filling and supervisory role of the Delaware courts. Given the simplified structure reflected in statutory portions of the mission statement and the diversity and strength of markets, private ordering, and norms discussed above, statutory changes are likely to be modest. Delaware may be at a point, however, where the existing statute does not sufficiently incorporate the current incentive structure for directors and managers, on which the rest of this system so depends. Delaware relies on experienced judges as a central part of the corporate governance system. Chancellor Chandler and Vice Chancellor Strine correctly illustrated the difference between Delaware corporate law and other lawmakers on issues of corporate governance: Delaware law comes "with a full-service commitment to enforcement." Most American corporate law is made by ten judges who work in Delaware. This dominance offers a real advantage to Delaware and corporate law alike, where corporate law is made by knowledgeable jurists who are repeat players on these issues and have an appreciation for what works.

III. SHARING THE MARKET FOR CORPORATE AND SECURITIES LAW-MAKING

A. Delaware and the Other States

Delaware, forty-ninth in size and forty-fifth in population among our fifty states, ranks first in the number of incorporations. More businesses, in fact, incorporate in Delaware than in all other states combined. Among

13The quotation is from the Delaware Supreme Court's opinion in Weinberger v. UOP, Inc., where the court recognized the Delaware block valuation technique in use for decades as "clearly outmoded" and authorized use of valuation techniques generally accepted in the financial community. Weinberger v. UOP, Inc., 457 A.2d 701, 712 (Del 1983). See also Unocal Corp. v. Mesa Petroleum Co., 493 A.2d 946, 957 (Del 1983) ("[O]ur corporate law is not static. It must grown and develop in response to, indeed in anticipation of, evolving concepts and needs.").

14See infra text accompanying notes 133-45.


16These are the five members of the court of chancery, who hear cases individually, but who regularly exchange views about corporate law, and the five justices of the supreme court who hear any appeals from the chancery court decisions in groups of three or five. Most major casebooks for teaching American law feature Delaware cases almost exclusively, at least as to the core questions of corporate governance.


America's largest corporations, including those that recently went public, Delaware holds an even larger share. The only relevant race is between Delaware and the home state where a company is located. When measured by each state's ability to attract corporations from out of state, the race is particularly one-sided in favor of Delaware. Only six other states have as many as twenty-five out of state incorporations and Delaware's share of all out of state incorporations exceeds eighty-five percent. This dominance is not likely to change. No other state can match Delaware in terms of reliability of its law and quick resolution of corporate disputes through the courts.

B. The Federal Government

Congress has consistently rejected federal incorporation. This reluctance does not mean that there is not federal competition for Delaware in the making of corporate governance rules. Various questions from time to time have attracted the attention of our federal legislators. Beginning in 1934, Congress chose to federalize part of the shareholder-director relationship, the officer-shareholder relationship. The Sarbanes-Oxley Act of 2002 contained new federal rules for the officer-director relationship. Specific examples of federal intrusion include rules relating to insider trading, solicitation of proxies, tender offers, and going private.

19Id. Table 2 shows Delaware with 57.75% of all firms, 59.45% of Fortune 500 firms, and 67.86% of firms going public 1996-2000.
20Id. at tbl. 5.
21Id.
22Theodore Roosevelt, Message of the President of the United States, Communicated to the Two Houses of Congress, at the Beginning of the First Session of the Fifty-Seventh Congress (Dec. 3, 1901), in THE WORKS OF THEODORE ROOSEVELT: 2 PRESIDENTIAL ADDRESSES AND STATE PAPERS 529, 544 "[T]he nation should, without interfering with the power of the States in this matter itself, also assume power of supervision and regulation over all corporations doing interstate business." See also 1 LOUIS LOSS & JOEL SELIGMAN, SECURITIES REGULATION 155-56 (3d ed. 1989) (describing certain Depression era corporate regulation bills in the context of the fledgling SEC).
24LOUIS LOSS, FUNDAMENTAL OF SECURITIES REGULATION 823 (1983) (thanks to Rule 10b-5, the minority rule under state common law as to insider trading has become the law of the land).
26See 113 CONG. REC. 854 (1967) ("[T]he need for such legislation has been caused by the increased use of cash tender offers rather than the regular proxy fight to gain control of publicly owned corporations . . . [t]his legislation will close a significant gap in investor protection under the Federal securities laws . . . .") (statement of Senator Williams); see also S. REP. NO. 550, at 3 (1967) (explaining the purpose is "to require full and fair disclosure for the
The chosen method of federal regulation usually has been disclosure. As such, federal law has long acknowledged its supplemental role to the states in allocating substantive rights among directors and shareholders. If this were the Academy Awards, Delaware and the feds would be in different categories: Delaware for leading roles and federal law for the supporting roles. Other constituencies have been diverted to other statutes, leaving corporate law focused on directors, shareholders and officers.27

C. How Much of Corporate Governance Does Delaware Decide?

Any discussion of the changes in corporate governance is best placed on an empirical base of how corporate disputes are currently resolved. This part presents a summary of recent studies of both federal and state decisions relating to challenges to corporate decisions. Stock exchange regulation is deferred until the following section.

1. Delaware Cases

To gain a picture of what Delaware corporate law is regulating today, my colleague Randall Thomas and I examined all complaints filed in the Delaware Court of Chancery for a two year period, 1999 and 2000.28 We found about 850 cases filed each year, of which seventy-five percent raised corporate issues.29 Of the corporate cases, almost seventy-eight percent raised questions of fiduciary duty and twenty-two percent raised statutory questions.30 The statutory category included several important and recurring areas of Delaware corporate law, such as Section 220, inspection of documents;31 Section 225, determination of director;32 Section 211, compelling the holding of shareholders' meetings;33 Sections 279 to 282, various questions relating to dissolution matters,34 and Section 262,

benefit of investors while at the same time providing the offeror and management equal opportunities to fairly present their case*).

27Roe, Delaware's Politics, supra note 4.
29Id. at 166 tbl. 1A.
30Thompson & Thomas, supra note 28, at 167 tbl. 1B.
31Id. at 167 tbl. 3, approximately thirty cases a year.
32Id. at 171 tbl. 3, approximately twenty cases a year.
33Id. at 167 tbl. 3, approximately ten cases a year.
34Thompson & Thomas, supra note 28, at 171 tbl. 3, approximately twenty cases a year.
2. Fiduciary Duty Cases

Fiduciary duty is the principal means by which the Delaware judiciary decides questions of corporate governance. These legal rules permit judges to apply core legal principles after the fact to a broad variety of situations in which managers may have misused the centralized power given them by the statutory structure described in the mission statement above. The Shareholder Litigation study, described above, reveals a surprising concentration of these claims: ninety-one percent of shareholder litigation in Delaware is against public companies; more than eighty-five percent of the fiduciary duty claims against public companies are class actions, with twelve percent derivative suits and seven percent direct actions; and ninety-four percent of the class actions arise out of acquisitions. Based on the above data, the dominant litigation type in Delaware is a class action against a public corporation challenging director action in an acquisition.

This study reveals several recurring patterns found in other types of representative litigation such as derivative suits or federal securities fraud class actions. This litigation is filed quickly, by a distinct set of plaintiffs' attorneys, in which there are usually multiple lawsuits arising from the same transaction. These suits are filed in all sorts of deals: third party arm's-length acquisitions, management buyouts (MBOs), cashouts by controlling shareholders, hostile bids or second bidders. Those suits that led to cash results, however, are concentrated in only one of these contexts—those where a controlling shareholder is implementing a cashout merger. There are a handful of MBO or third party merger cases producing relief, yet most of these cases are dismissed with no monetary

35Id. at 171 tbl. 3, only about ten cases a year; Del. Code Ann. tit. 8, §§ 211, 220, 225, 262, 279-82 (2001).
36Thompson & Thomas, supra note 28, at 169 tbl. 2. The numbers in the second claim add up to more than 100% because some complaints include both class and derivative counts or other overlaps.
37Id. at 182, 183 tbl. 9. More than two-thirds of lawsuits filed within three business days of the transaction generating the controversy.
38Id. at 185. Sixteen firms were a party to more than three-fourth of the lawsuits.
39Id. at 183-84 & tbl. 10. There was an average of about four suits per transaction for the class actions with many transactions generating ten or more lawsuits.
40Thompson & Thomas, supra note 28, at 175 tbl. 5.
41Id. at 199 & tbl. 17. Control shareholder transactions, which made up about thirty percent of the consolidated or lead complaints, produced almost two-thirds (twenty of thirty-one) of the lead cases that produced monetary relief.
recovery.\textsuperscript{42} Additionally, there was no monetary recovery in any of the hostile bid or second bidder cases.\textsuperscript{43} Many cases raised a Revlon issue but none produced any relief.\textsuperscript{44} Almost none of the cases raised a Unocal issue.\textsuperscript{45} Weinberger claims are the one set of cases where relief occurs.\textsuperscript{46}

While relief in fiduciary duty cases was confined principally to cashout cases, we found that not all cashout cases produced monetary relief. When we broke down the category of cashout cases into those that led to monetary relief and those that were dismissed without any monetary relief, we found that the initial premium offered in the cases that produced relief were lower than the premiums that had been offered in the cases where the litigation was subsequently dismissed without payment.\textsuperscript{47} This difference was statistically significant.

In contrast to the class actions, the derivative suits filed in Delaware arise in nonacquisition settings.\textsuperscript{48} As noted above, class actions outnumber derivatives by an eight to one margin.\textsuperscript{49} After taking into account the multiple lawsuits arising out of the same transactions, there were less than thirty derivative cases per year in Delaware against public companies.\textsuperscript{50} A significant majority of derivative cases raise conflict of interest or duty of loyalty questions.\textsuperscript{51} Some cases pose duty of care claims, a category where the result is limited by the exculpatory blanket provided by the Delaware statute.\textsuperscript{52} Those claims that are not conflict issues tend to be failure to

\textsuperscript{42}Id. at 199 tbl. 17. There were about eleven cases in these two categories that produced monetary relief.

\textsuperscript{43}Id.

\textsuperscript{44}Thompson & Thomas, supra note 28, at 195 tbl. 15. There were 233 complaints raising a Revlon issue, the director's duty to get the best price for shareholders in an acquisition setting. See Revlon, Inc. v. MacAndrews & Forbes Holdings, Inc. 506 A.2d 173, 175 (Del 1986).

\textsuperscript{45}Thompson & Thomas, supra note 28, at 195 tbl. 15. Only ten cases in the entire data base raised a Unocal issue and none produced affirmative relief. Unocal refers to the enhanced scrutiny that the Delaware court provide when a challenge is raised to a defensive tactic in a takeover. See Unocal Corp. v. Mesa Petroleum Co., 493 A.2d 946 (Del. 1985).

\textsuperscript{46}Thompson & Thomas, supra note 28, at 195 tbl. 15. See Weinberger v. UOP, Inc. 457 A.2d 701, 703 (Del. 1983) (applying an entire fairness standard when a controlling shareholder implements a merger that cashes out the minority shareholders).

\textsuperscript{47}Thompson & Thomas, supra note 28, at 201 tbl. 18. Those deals in which subsequently produce additional payment offered an initial deal premium of fifteen percent, while those deals in which subsequent litigation was dismissed without additional cash payments reported an initial deal premium of 25.5%.

\textsuperscript{48}Id. at 169 tbl. 2 (ninety percent of derivative complaints (123 of 137) arise in non-acquisition settings).

\textsuperscript{49}Id.

\textsuperscript{50}Id.

\textsuperscript{51}See Thompson & Thomas, supra note 28, at 143.

\textsuperscript{52}DELCODE ANN. tit. 8, § 102(b)(7) (2001).
supervise frequently linked with claims alleging insufficient financial records. Derivative cases generally take longer to settle so our disposition results remain incomplete as compared to the class action cases.\textsuperscript{53}

In summary, Delaware litigation is surprisingly limited in the types of issues resolved. The cases are overwhelmingly focused on acquisitions and, particularly, conflict of interest in acquisitions. This litigation pays some attention to conflicts of interest elsewhere and certain statutory cases, yet the overall picture focuses on a few discrete areas of corporate governance that are more limited and occur more sporadically than might be expected for a plenary governance system.

D. Compared to Federal Securities Regulation

Delaware's litigation can not be completely understood without looking at corporate governance litigation in federal courts. Professor Hillary Sale and I undertook a study of federal securities fraud complaints filed in 1999, to see what part of corporate governance was before federal judges.\textsuperscript{54} The study focused on complaints filed in three circuits, the Second, Third, and Ninth, which together produced about half of the complaints for that year.\textsuperscript{55}

Federal litigation consisted entirely of class action suits filed in district courts, predominately claiming Rule 10b-5 violations.\textsuperscript{56} In contrast to Delaware where plaintiffs filed suit exclusively against directors, the target of federal class actions are officers and the company itself.\textsuperscript{57} Of the eighty-two cases that named individual defendants in addition to the company, eighty-one named the CEO and two-thirds named the CFO.\textsuperscript{58} In the twenty-one cases where the directors sued were not one of the corporation's chief officers, a majority of these suits included claims based on section 11 of the 1933 Act or another section that provides a specific

\textsuperscript{53}Thompson & Thomas, supra note 28, at 186.
\textsuperscript{54}Robert B. Thompson & Hillary A. Sale, Securities Fraud as Corporate Governance: Reflections upon Federalism, 56 VAND. L. REV. 859, 890 (2003); 1999 was one of the years covered previously in the state study.
\textsuperscript{55}Id. The Second and Ninth Circuits are the most prominent circuits today for securities litigation. The Third circuit, in addition to itself having a large number of important securities cases, also takes in Delaware, the subject of the state law study described earlier. Those three circuits represented about half of the securities fraud class action for that year. Our sample, after excluding those that were not relevant or could not be obtained, was made up of eighty-six complaints.
\textsuperscript{56}Id.
\textsuperscript{57}Id. at 895.
\textsuperscript{58}Thompson & Sale, supra note 54, at 896 tbl. 3.
statutory remedy against directors.  

A chief executive officer who is also a director may not focus on which capacity the suit names, but the point here is that there is some separation and specialization in what the federal courts are doing and what Delaware is doing. A comparison of the lawsuits filed in the two systems reveals a shift in the pattern of corporate governance litigation that should concern Delaware. First, disclosure has emerged as a key mechanism of corporate governance, a trait primarily associated with federal law. Such transparency facilitates the efficient operation of various markets, enables auditors and analysts to monitor corporations more effectively, and assists directors in their own monitoring role.

Second, through its focus on disclosure, federal law highlights the role of officers, in contrast to Delaware's traditional concentration on directors. In our increasingly complex economy, officers occupy a greater role in corporate governance. Federal lawmakers have not been willing to leave officer conduct to the discretion of directors and to market constraints as Delaware has done.

Third, disclosure provides an accessible vehicle for judges to evaluate duty of care claims against officers and directors, which have been foreclosed to most Delaware litigants since the enactment of Section


60It is not just mandatory disclosure, which under Regulation S-K now covers sixty items and over 100 pages in the federal rule book, but it is the increasingly intrusive obligations that disclosure now covers. For example, a company must disclose: it has a Code of Conduct and if not, why not; if its board nominating committee has a charter and if not, why not. 17 C.F.R. §§ 229.10-101b (2003). See generally Lawrence A. Hamermesh, Calling Off the Lynch Mob: The Corporate Director's Fiduciary Disclosure Duty, 49 VAND. L. REV. 1087 (1996) (discussing parallel disclosure obligation under federal statutes and state common law). The new obligations on officers are discussed in more detail below.

61Thompson & Sale, supra note 54, at 905.

62Alan Greenspan, Excerpts from Report by Greenspan at Senate, N.Y. TIMES, July 17, 2002, at c8, col. 5 ("[V]ast and highly liquid financial markets enable large institutional shareholders to sell their shares when they perceive inadequacies of corporate governance, rather than fix them. This has placed de facto control in the hands of the chief executive officer.").

A common thread in federal lawsuits is nondisclosure. Plaintiffs in federal court frequently file suit after unexpected news and a subsequent price drop. The substance of the complaint usually relates to the management of the business, which would be brought as a care claim if filed in Delaware. Federal law, therefore, has come to occupy one of the core spaces of fiduciary duty.

Fourth, federal class actions have emerged as a close substitute of derivative suits for enforcing corporate governance issues. In such a contest, federal suits present some advantages. Federal class actions offer a more accessible damage formula and perhaps, a better handle litigation agency costs inherent in such representation.

Prior to the reforms initiated by the Sarbanes-Oxley Act, federal law had steadily occupied a larger role in the corporate governance realm. The enactment of Sarbanes-Oxley and related rules propelled federal law to its current position as the dominant regulator of officer conduct. Federal law has become the most likely source of law for governing duty of care issues. Delaware's long-held preference has been to leave those areas clear for whatever private ordering the directors may find appropriate. The continued silence by Delaware risks ceding much of this part of corporate governance to federal law.

IV. THE CHALLENGE TO DELAWARE FROM THE POST-ENRON REFORMS

Enron and the scandals that followed it prompted an increased scrutiny of corporate governance that seems to emerge every decade or so

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65 Thompson & Sale, supra note 54, at 893 tbl. 1 (recording the drop in value reported in forty-eight complaints).

66 Id. at 898 tbl. 4 (revealing that eighty-eight percent of complaints alleged misrepresentations about earning, sales, or production problems tied to a failure to meet earnings prediction; forty-three percent, including some that overlapped with the prior category, alleged misrepresentations related to acquisitions).


68 The Private Securities Litigation Reform Act of 1995 imposed new rules permitting judges to select the class attorney and prohibiting individual plaintiffs from bringing an excessive number of suits, provisions that go beyond current Delaware law in dealing with representative litigation brought as derivative suits. 15 U.S.C. § 74u-4 (2000).
with a more intense experience in each generation. What we have experienced in the last two years is something like a hundred year flood of reform. Three parts of this most recent reform affect Delaware: (1) Congressional legislation—the Sarbanes-Oxley Act; (2) the new New York Stock Exchange listing standards and parallel Nasdaq standards; and (3) the SEC's proposed rule-making regarding the role of shareholders in director nominations. All three intrude into the traditional area of corporate governance regulated by Delaware.

A. The Sarbanes-Oxley Act of 2002

The most recognizable part of Sarbox was the increased federal role in regulating accountants or auditors, attorneys and analysts. These rules, however, do not directly impinge on Delaware corporate law as reflected in the mission statement set out at the beginning of this article. These gatekeepers certainly impact governance, yet their regulated activities are not central to the model that Delaware follows.

There are parts of the new federal regime, however, that overlap Delaware law, particularly those sections that define the roles of directors and officers beyond what federal law had done in the past. As to directors, Sarbox specified the function of the audit committee of the board. The legislation required that all members of the committee be independent and that at least one member be financially literate. Those rules are not inconsistent with Delaware law, but Delaware does not require an audit committee nor does it impose qualifications for any director. Thus by

70Id. § 307. This led to SEC Regulations on "Standards of Professional Conduct for Attorneys Appearing and Practicing before the Commission in the Representation of an Issuer" See 17 C.F.R. § 205.1 to 205.7 (2003).
72The Sarbanes-Oxley Act of 2002 § 301, amending § 10A(m)(3) of the 1934 Act (requiring each member of the audit committee be independent).
73The Sarbanes-Oxley Act of 2002, § 407 (requiring the SEC to issue rules that issuers disclose "whether or not, and if not, the reasons therefor, the audit committee of that issuer comprised of at least 1 member who is a financial expert, as such term is defined by the Commission"). See Standards Relating to Listed Company Audit Committees, Release Nos. 33-47654, 33-8220 (Apr. 25, 2003), available at http://www.sec.gov/rules/final/33-8220.htm (adding, among other provisions, Item 401(h) to Regulation S-K and Item 7(d)(3) to Schedule 14A (codified at 17 C.F.R. §§ 229.401, 240.14a-101, respectively).
74Del. Code Ann. tit. 8, § 141(c) (2001) permits the board to designate one or more committees, but does not require any. Directors' qualifications are not specified other than that they be natural persons. Section 141(b) negates any statutory requirement that they be shareholders.
enacting those sections of Sarbox, Congress has, for the first time, taken away the right of Delaware to leave this space vacant and to let private ordering determine the appropriate means by which directors do their jobs.

Additionally, Congress has imposed several specific obligations on officers, requiring: (1) certain high ranking officers to certify financial statements,75 (2) the corporation's attorneys to report to the chief legal officer or the chief executive officer about breaches of fiduciary duty,76 (3) the CEO to certify whether controls in place are effective,77 and (4) a code of conduct for senior financial officers or an explanation as to why the company lacks one.78 Again, these requirements do not conflict with any affirmative requirement of Delaware law. Recall, however, that Delaware law discusses officers sparingly and says nothing about what they must do. Section 142 refers to officers but the section defers almost completely to the corporation's bylaws or board resolutions as to what officers should do, how they are chosen, and how vacancies are filled.79 This new federal law now constricts the space that Delaware has given directors to define or not define what the directors want the officers to do.

B. New Listing Standards by Stock Exchanges

The new listing standards proposed by the New York Stock Exchange and NASDAQ in 2002 and approved by the SEC in November 2003 are a more direct intrusion into Delaware's governance space.80 These standards ostensibly come from quasi-private groups, which, in the case of the New York Stock Exchange has been making rules about corporate governance much longer than the federal government and long before Delaware assumed center stage in corporate law.81 This history, however,

75 See The Sarbanes-Oxley Act of 2002 § 401.
76 Id. § 307.
77 Id. § 404.
78 Id. § 406.
79 Del. Code Ann. tit. 8, § 142(b) (2001); see supra Part IV.A.
81 See Securities Exchange Act of 1934, § 3(a)(26), 15 U.S.C. § 78c(26) (2000) (defining self-regulatory organization to mean any national securities exchange or registered securities association). The New York Stock Exchange is a national securities exchange. Nasdaq has sought SEC approval to be recognized as an exchange but no action has yet been taken so that Nasdaq's governance listing requirements have a hybrid status that derives from Nasdaq's prior association with the National Association of Securities Dealers, which is a registered securities association under the definition. See John C. Coffee, Jr., Racing Toward the Top?: The Impact of Cross-Listings and Stock Market Competition on International Corporate Governance, 102
paints a misleading picture. The current set of regulations differs from the historic NYSE listing standards and has much more of the appearance of an indirect way for the SEC to operate in a manner that a federal appellate court in the Business Roundtable case said the federal agency could not.\footnote{Business Roundtable v. SEC, 905 F.2d 406, 407 (D.C. Cir. 1990).}

1. The Current Changes as Core Corporate Governance

The new listing standards require that at least a majority of a corporation's directors as well as all members of the audit, compensation, and governance committees be independent as that term is defined in the standards.\footnote{NEW YORK STOCK EXCHANGE LISTED COMPANY MANUAL § 303A.01-06 (2003), available at http://www.nyse.com/listed/p1020656066790.html?displayPage=/listed/102065606790.html (last visited Oct. 4, 2004).} The rules as to audit committees were overtaken by the Sarbox changes.\footnote{The Sarbanes-Oxley Act of 2002 §§ 201-209. The report of the NYSE committee to its board in June 2002 required that the audit committee be composed entirely of independent directors. By the time this was approved by the NYSE board and sent to the SEC for approval, Sarbanes-Oxley had intervened with a more stringent standard. Standards Relating to Listed Company Audit Committees, Release Nos. 33-8220, 34-47654 (Apr. 25, 2003), available at http://www.sec.gov/rules/final/33-8220.htm. NASDAQ proposed revisions to its listing requirements requiring boards to have a majority of independent directors and for directors to meet without company management. See Pending Corporate Governance Rule Filings, at http://www.nasdaq.com/about/Proposed rules.stm#boards (last visited Oct. 4, 2003).} All of these changes provide rules at the core of corporate governance and a rule about which Delaware law is silent. The listing standards also specify how directors should do their job, specifically requiring meetings without the CEO and with a lead director.\footnote{NEW YORK STOCK EXCHANGE LISTED COMPANY MANUAL, supra note 83, § 303A.03.} The changes also increase the role of shareholders by requiring shareholder approval of compensation plans.\footnote{Id. § 303A.08.}

2. How They Compare to Historic NYSE Listing Standards

The NYSE initially made individual listing agreements with their listed companies in the nineteenth century and included governance standards with financial requirements before the enactment of general incorporation statutes. Essentially there have been three spurts of activity as to listing standards on core governance issues.

The first spurt occurred in the years leading up to the 1934 Act. The
NYSE had required annual reports by the turn of the century,\textsuperscript{87} semiannual reports by 1917, and quarterly reports by 1923.\textsuperscript{88} In 1926, the NYSE added an important governance provision in terms of the prohibition on dual class voting.\textsuperscript{89} Six years later, the NYSE required certification of financial statements.\textsuperscript{90} Such listing standards were developed primarily to provide guidance as to what was to go into individual listing agreements; they were typically not binding on companies that listed prior to the inception of the particular standards. The Securities Exchange Act of 1934 incorporated most of these requirements,\textsuperscript{91} and there was a period of quiescence as to listing standards until the 1950s.\textsuperscript{92} Note that except for dual class these were not issues that came within Delaware's core mission in regulating corporate governance.

During the 1950s, the NYSE made a series of changes to its listing requirements that revealed a different pattern. In 1953, the NYSE required a quorum for shareholders' meetings.\textsuperscript{93} In 1955, shareholder approval of conflict transactions or issuance of significant additional shares was

\textsuperscript{87}GILBERT W. COOKE, THE STOCK MARKETS 340 (rev. ed. 1969). This effectiveness of this requirement was qualified because until 1910 listing was not a requirement for trading on the exchange.

\textsuperscript{88}Id. It was further mandated that both income statements and balance sheets be included in these reports.

\textsuperscript{89}See Special Study Group of the Committee on Federal Regulation of Securites, American Bar Ass'n, Section of Bus. Law, Special Study on Market Structure, \textit{Listing Standards and Corporate Governance}, 57 BUS. LAW. 1487, 1503 (2002). \textit{See also} Banker's Control of Trade Deplored', N.Y. TIMES, Oct. 29, 1925, at 27 (commenting on the problem of non-voting or diluted voting stock and how the sale of such stock centralized the corporate power in the hands of a few fraction of the shareholders). The following year the reaction to the NYSE's announcement of a listing by Dodge Brothers, Inc. with a dual class structure propelled the adoption of the NYSE standard. \textit{See generally} Joel Seligman, \textit{Equal Protection in Shareholder Voting Rights: The One Common Share, One Vote Controversy}, 54 GEO. WASH. L. REV. 687 (1986) (tracing the evolution of the NYSE policy).

\textsuperscript{90}GEORGE L. LEFFLER & LORING C. FARWELL, THE STOCK MARKET 140 (3d ed. 1963) (Loring C. Farwell rev., Ronald Press Co. 3d ed. 1963) ("In April, 1932, the Exchange made the 1928 policy of independent audits mandatory for all new companies applying for listing.").

\textsuperscript{91}See, e.g., Securities Exchange Act of 1934, §§ 13-14, 16 (codified as amended at 15 U.S.C. §§ 78(m), (n), & (p) (2000)).

\textsuperscript{92}Douglas C. Michael, \textit{The Untenable Status of Corporate Governance Listing Standards Under the Securities Exchange Act}, 47 BUS. LAW. 1461, 1469 (1992) ("With one minor addition, the extension of minimum voting rights to preferred stock in 1940, the NYSE's corporate governance listing standards had remained essentially unchanged from 1926 [to the 1950s].")

\textsuperscript{93}Id. at 1469 n.43 (citation omitted).
required.94 Two outside directors were required a year later.95 In 1959, a provision was added mandating the solicitation of proxies for shareholder meetings and one year later a new term addressed disclosure of change in control.96 These requirements addressed what would be expected to be a part of a state's corporate governance law, yet they only applied to NYSE companies. This spurt of changes in the 1950s seems to have been inspired by the NYSE's effort to attract business from everyday investors and achieve a brand name effect for its stocks in appealing to those investors.97 The SEC was less visible at this time, its employment having dipped to its lowest level since the agency's infancy.98

The third or modern period of listing standards began in the late 1970s and continues today. There have been four notable areas of listing standards in this period: (1) one share/one vote—a series of events unfolding between 1984 and 1994;99 (2) requirements for audit committees

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94Id. See also LOUIS LOSS & JOEL SELIGMAN, 4 SECURITIES REGULATION 1827 n.270 (3d rev. ed. 1990) (describing November 1955 action by the NYSE Board of Governors based on an increase in outstanding shares of twenty percent or more); see NEW YORK STOCK EXCHANGE LISTED COMPANY MANUAL § 312.03(c), supra note 83, § 312.03(c).

95Michael, supra note 92, at 1469.

96Id. (quoting releases in 1959 and 1960 respectively announcing listing standards regarding mandatory solicitation of proxies and additional shareholder voting requirements).

97Id. at 1469-70. See also ROBERT SOBEL, N.Y.S.E., A HISTORY OF THE NEW YORK STOCK EXCHANGE 1935-1975, at 199-200 (1975) (discussing this effort).

98See LOSS & SELIGMAN, supra note 22, at 301 n.23 (reporting staff size on a yearly basis dipping to 667 in 1955).

99Seligman, supra note 89, at 704; Voting Rights Listing Standards; Disenfranchisement Rule, Exchange Act Release No. 34-25,891, 53 Fed. Reg. 26,376 (July 12, 1988); 17 C.F.R. § 240.19c-4 (2003); Business Roundtable v. SEC, 905 F.2d 406, 407 (D.C. Cir. 1990); see Special Study Group, supra note 89, at 1505-06 (quoting then SEC Chairman Breeden) (describing SEC efforts to first get the NYSE to adopt a rule, then the NASDAQ, but resistance by the Amex leading to a suggestion by the SEC chair that "Congress 'consider identifying minimum federal protections for voting rights"); Amy L. Goodman, One Share/One Vote . . . Again, 5 INSIGHTS 2 (1991) (describing additional pressure from the Council of Institutional Investors and others on the Exchanges).
inserted first in 1977,\textsuperscript{100} revisited in 1998,\textsuperscript{101} and again in 2002,\textsuperscript{102} (3) shareholder approval of compensation that evolved from 1998 through 2002;\textsuperscript{103} and (4) director independence, lying at the heart of the rules approved by the SEC in 2003.\textsuperscript{104} These four sets of regulations directly address matters within Delaware's traditional core of corporate governance: the roles of directors, shareholders, and officers. The dominant player in the process was the SEC, not the NYSE. In three of the four sets of changes, in fact, it was a call or letter from the chair of the SEC that got the ball rolling.\textsuperscript{105} They do not bubble up from within the exchange.\textsuperscript{106} The SEC has worked each time to prevent the exchanges from competing among themselves as to the regulation of these areas. The exchanges' incentives to provide any such governance rules has diminished as technology fundamentally reshaped how exchanges work and provided alternatives to the exchanges for trading and for rules on corporate


\bibitem{101} \textit{See generally} Special Study Group, \textit{supra} note 89, at 1507-09 (describing the events in 1998 that involved audit committees).

\bibitem{102} The Sarbanes-Oxley changes instituted in part because of Enron and the other prominent corporate scandals.


\bibitem{104} \textit{See supra} note 80.

\bibitem{105} SEC Chairman Arthur Levitt, Jr., The "Numbers Game," Remarks at the NYU Center for Law and Business (Sept. 28, 1998), \textit{available at} http://www.sec.gov/news/speech/speecharchive/1998/spch220.txt (calling for an improvement in the auditing procedures); SEC Chairman Arthur Levitt, Jr., Remarks at the 2000 Annual Meeting of the Securities Industry Association (Nov. 9, 2000), \textit{available at} http://www.sec.gov/news/speeches/spch420.htm (urging the markets "to restore promptly the rightful balance between shareholder and management interests by requiring shareholder approval for all plans that grant options or award stock to officers and directors"); and Harvey Pitt, Remarks at the Inaugural Lecture of the JD/MBA Lecture Series, Kellogg Graduate School of Management and Northwestern Law School (Apr. 4, 2002), \textit{available at} http://www.sec.gov/news/speeches/spch547.htm (commenting on audit committees, shareholder approval of compensation, and director independence). "We will have to make it clear ... that although it was a request, it was expected to be implemented. They should move with alacrity."

governance. Without the SEC's leadership, the exchanges would not likely have entered into the arena of corporate governance. These rules, therefore, merit a closer examination of their impact on the line between federal and state regulation of corporate governance.

3. Moving the Line that Divides Federal and State Regulation of Corporate Governance

These changes have moved the line between federal and state regulation of corporate governance adding more to the federal realm. The Supreme Court declared in *Santa Fe Industries, Inc. v. Green* that "[a]bsent a clear indication of congressional intent, we are reluctant to federalize the substantial portion of the law of corporations that deals with transactions in securities, particularly where established state policies of corporate regulation would be overridden." In *Business Roundtable v. SEC,* a panel of judges on the D.C. Circuit blocked SEC Rule 19c-4 that had prohibited dual class shares since it was not a function delegated to the agency by the 1934 Act. The *Business Roundtable* opinion concluded with a pointed rebuke to the SEC, "Wrong court, bad gamble." The court, however, preserved the ability of the exchanges to issue their own rules, which the SEC actually approves. So the SEC worked to bring one share/one vote within this permissible area of regulation and after four years was able to get all of the exchanges to adopt a similar rule. Since 1994 we have had exchange labeled and SEC approved rules that ban new dual share voting. Using the exchanges, the SEC moved the line of federal regulation deeper into the state-dominated realm than the agency would have been permitted to do alone under *Business Roundtable.*

C. Proposed SEC Rules on Shareholder Access to the Nomination Process

The current SEC proposal reflects the most recent shift in the line between federal and state regulation of corporate governance. This current

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108905 F.2d 406 (D.C. Cir. 1990).
109Id. at 407.
110Id. at 416.
111Id. at 414-15.
proposal seeks to permit shareholders, particularly institutional shareholders, greater access to the ballot when directors are elected.\textsuperscript{114} There is no question more central to state corporate law than the ability of shareholders to elect directors.\textsuperscript{115} Federal regulations govern the disclosure that must be made whenever shareholder proxies are sought, but that regulation has not decided the questions on which those holders are permitted to exercise their franchise.\textsuperscript{116} Rule 14a-8 has long provided an apparent substantive federal right for shareholders to specify items to be included on the agenda for a shareholder's meetings at the corporation's expense.\textsuperscript{117} In an apparent nod to the substance determining role of state law, the federally-provided agenda access is only available where the proposal would be a proper subject for shareholder action under state law.\textsuperscript{118} The agency then provides its own interpretation of state law: even where state law provides no express shareholder power they have advisory power to express views that are not binding on the board.\textsuperscript{119} By this indirect suggestion, and state law silence in response to it, federal law has evolved to provide access to the proxy on a host of questions.\textsuperscript{120} Current proposals would provide additional rights for shareholders in the election process. Subject to several important conditions concerning director unresponsiveness to shareholder opinion, shareholders would be


\textsuperscript{115}See Blasius Indus., Inc. v. Atlas Corp., 564 A.2d 651, 659 (Del Ch. 1988) (emphasizing shareholder voting is "critical to the theory that legitimates the exercise of power by some... over vast aggregations of property that they do not own").

\textsuperscript{116}Business Roundtable v. SEC, 905 F.2d 406, 411 (D.C. Cir. 1990) ("In 1934 Congress acted on the premise that shareholder voting could work, so long as investors secured enough information and, perhaps, the benefit of other procedural protections. It did not seek to regulate the stockholders' choices.").

\textsuperscript{117}17 C.F.R. § 240.14a-8 (2003).


\textsuperscript{119}Id. § 240.14a-8(h)(3)(i)(1), note to para. (i)(1) ("[A] proposal drafted as a [mere] recommendation or suggestion is proper unless the company demonstrates otherwise."). The SEC has long recognized the tentative nature of the shareholder right it purports to provide. See Securities Exchange Act Release 12,598, 9 SEC Docket 1033 (1976) (proposed), 10 SEC Docket 1006, 1010 (1976) (adoption).

\textsuperscript{120}There are hundreds such proposals each year.
able to have a partial slate of nominees for directors included on the corporation's ballot.\textsuperscript{121} The proposal, therefore, is directed toward protecting the voice of the shareholder, not the command of the board. The proposal functions in a manner similar to cumulative voting, which traditionally has permitted inclusion on the board of minority members.\textsuperscript{122} Cumulative voting, however, stems from state law. How can this federal proposal be consistent with the role of federal regulation in corporate governance?

The reasoning is an expanding series of analogies. First, federal law permits disclosure to make the shareholder franchise more effective and to prevent the seeking of proxies from shareholders without full disclosure.\textsuperscript{123} Second, Rule 14a-8, with the benefit of sixty years of history, grants shareholder access to the issuer's proxy statement for resolutions they could make if they attended the annual meeting.\textsuperscript{124} Proxy rules inserted over a decade ago prevent management from bundling proposals that are presented to shareholders.\textsuperscript{125} How is that different from the board's authority to establish the time and place of the meeting? Rules from the 1992 revision require a method for shareholders to submit their own candidate without having to provide a full slate.\textsuperscript{126} This current proposal extends shareholders' process rights. If shareholders have the right to write in, why should they not have the right to nominate?

Shareholders probably should have the right. Yet for this to be included in federal rules would show just how deep an intrusion into state law the federal government has made. This would be an unprecedented extension of federal authority without any Congressional authorization.

\footnotesize{\textsuperscript{121}See Proposed Rule 14a-11, supra note 114.}

\footnotesize{\textsuperscript{122}See HARRY G. HENN & JOHN R. ALEXANDER, LAWS OF CORPORATIONS 495 (3d ed. 1983) ("Cumulative voting is a form of proportional representation to assure any desirable minority representation on the board.").}

\footnotesize{\textsuperscript{123}See J.I. Case Co. v. Borak, 377 U.S. 426, 431 (1964) (Section 14(a) intended to "control the conditions under which proxies may be solicited with a view to preventing the recurrence of abuses which . . . [had] frustrated the free exercise of the voting rights of stockholders.") (quoting H.R. Rep. No. 1383, 73d Cong., 2d Sess. 14).}

\footnotesize{\textsuperscript{124}See LOSS & SELIGMAN, supra note 94, at 1933-40 (describing the evolution of Rule 14(a) since its inception in 1935 and commenting that the evolution was designed to the closest substitute to actual attendance).}


\footnotesize{\textsuperscript{126}Id. at 83,371-83,372 (revising Rule 14a-4 to permit voters to fill out their own partial slate with management nominees).}
The SEC seems undeterred by the presence of Business Roundtable.127 This proposal like that of Rule 14a-8 seems to acknowledge state law because the federal rules only apply if shareholders have the right under state law to nominate directors.128 But this apparent deference is sharply limited by a presumption that shareholders have this power unless state law says they do not. This denial of rights to shareholders would be a strange thing to find in state law. Recall that all state corporations statutes including Delaware allocate all corporate power to directors and specify only a very few limited rights for shareholders.129 There would be no reason to have an exception as to what shareholders cannot do in such a system, but that silence has become the basis for the federal agency to create a positive right for shareholders.

V. POSSIBLE DELAWARE RESPONSES

When the corporate scandals of the post-bubble economy were revealed, the major competitors to Delaware in regulating corporate governance, i.e., Congress, the stock exchanges and the SEC, responded in a more dramatic fashion. The Business Roundtable responded more than Delaware;130 even the American Bar Association Task Force responded more than Delaware.131

Of course, the fact that Delaware has not responded does not mean these reforms are correct. Sarbox, in fact, has been criticized as being unresponsive to the abuses that begat this crisis, particularly the excesses of executive pay and the perverse incentive to misreport financial results because of those excesses.132 The federal statute, rather, collected various then-existing reform proposals. We should not, however, underestimate the change in auditor behavior that will follow from the new law. The stock exchange listing standards incorporate good practices that most Delaware corporations follow, pursuant to the advice of Delaware lawyers and

127 Business Roundtable v. SEC, 905 F.2d 406, 411 (D.C. Cir. 1990) ("If the Commission believes that premise [that Congress did not seek to regulate substance is] misguided, it must turn to Congress.").
128 See Proposed Rule 14a-11, supra note 114.
129 See generally DEL. CODE ANN. tit. 8, § 141 (2001) (enumerating the power of the board of directors).
direction from the Delaware judiciary in their ongoing interpretations of fiduciary duty.

The strongest argument for a non-response response may be that the abuses that generated our recent crisis arose in the hyperventilated atmosphere of the late bubble economy. Alan Greenspan commented that in such a setting, our traditional protectors against fraud were overwhelmed.133 The American economy, of course, cooled down and some of the incentives that so provoked the excesses of the recent period have since disappeared. The psychological setting of a later bubble economy that facilitated some of the abuses has also receded. In this cooler setting, it may be that the traditional guardians will once again be up to the challenge. If abuses remain the Delaware approach, of allowing directors to use all of the various incentives, monitors, and norms, could make the necessary adjustments without express legal changes.

Is there a downside to a status quo response in Delaware? There is, if Delaware's response would halt the intrusions from these other sources. Two facts are relevant. First, the New York Stock Exchange is not likely to have the same role in corporate governance that it held in the last year. Technological changes and market shifts have dulled both its incentives and ability to make corporate governance rules.134 Second, the SEC is at the edge of its statutory authority. Congress is not likely to revisit the question in the near term. Timely action by Delaware can apply new pressure on the SEC and the NYSE to retreat from the questionable authority they now seek to apply. Delaware, as it has done before, should consider a more proactive approach that would make Congress, the NYSE, the SEC, and the courts more comfortable in forgoing additional regulation and adhering to the traditional division of corporate governance.

Delaware's General Corporation Law, the linchpin of state law, is fraying around the edge. Its 1967 revision commanded the attention of the most knowledgeable group of Delaware lawyers and received the admiration of successive members of the Delaware bar committee and the legislative committees, yet much has changed since the mid 1960s.135 Given the evolving nature of corporate law, many points lying at the core of corporate governance are not covered in the current statute:

133Greenspan, supra note 62, at c8.
134See Craig Pirrong, A Theory of Financial Exchange Organization, 43 J. L. & ECON. 437 (2000) (analyzing, from an economic point of view, the effect that organization and corporate governance have on securities exchanges).
• **Officers**

Given the important role of officers in the modern corporation, the silence of the Delaware General Corporation Law about officers is deafening. Delaware law focuses on the prominent role of directors in corporate governance. As long as directors are also officers, legal constraint on directors would reach senior management. As corporations shift to boards with only one officer as a member, it becomes more important to focus on the legal regulation of officers separate from directors. The recently passed long-arm statute is a step in the right direction which permits the Delaware courts to enforce existing fiduciary duties against officers.136 Any minimal reform of the General Corporation Law ought to reflect the central place that the CEO occupies.

• **Directors**

There has been a massive shift in the census of directors since the time of the last Code revision. Independent corporate directors have demonstrated staying power such that it cannot be described as a fad. To omit such a requirement from a corporate code suggests a system that is out of touch with modern reality.

• **Shareholders**

Similarly there has been a massive shift in the census of shareholders since the time of the last revision. Any minimal change to the General Corporation Law would recognize the presence of institutional shareholders and suggest voting changes consistent with their presence. There is no reason to allow the feds to decide who gets the right to vote. A thoughtful response from Delaware, therefore, could render some of the existing and proposed federal regulations moot.

• **Appraisal**

Perhaps the most out-of-date provisions in the current statute are the appraisal and acquisitions sections. The structure of the appraisal statute and much of its substance dates from a time when the statute was directed toward minority shareholders who had been offered the opportunity to continue in the enterprise after an arm's-length merger but who desired to

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exist and receive fair value from the corporation.\textsuperscript{137} This context generates very few appraisal cases today. The overwhelming use of appraisal is in the cashout setting where the controlling shareholder forces the minority shareholders out of the business, based on the terms set by the majority.\textsuperscript{138} Delaware law's transition from the first context to the second has been dramatic in the last thirty years and has resulted mostly from judicial action, thereby leaving the statute confusing and misdirected.

Consider Section 262 of the Delaware's Corporate Law.\textsuperscript{139} Subsection (b) states the general rule that appraisal is available to the shareholders of each constituent corporation in a merger.\textsuperscript{140} Subsection (b)(1) provides an exception that strips shareholders of their appraisal rights, when there is a sufficiently deep and liquid market.\textsuperscript{141} Certainly there is no reason for law to provide a remedy when the market can do it cheaper, particularly in an arm's-length merger where the market price likely reflects full information about the company. Subsection (b)(2), which is an exception to the exception, creates a double negative that equals a positive and returns appraisal rights to some shareholders of a publicly held corporation.\textsuperscript{142} So what subset of cases is covered by this exception to the exception? Due to the fact that this subset is defined in the negative, this point is practically impossible to follow. The shareholder gets appraisal unless receiving stock or other named kinds of consideration. It is not at all apparent that appraisal is intended as a check on majority shareholders setting their own terms for getting rid of the minority. Appraisal in this setting is a seldom used remedy.\textsuperscript{143}

\section*{VI. Conclusion}

The challenge to Delaware is not the possibility of an imminent decline in fees that incorporations contribute to the state budget. Delaware has won the race to the bottom, or top, in competition with other states and that is not likely to change in the foreseeable future. Continuing on the

\textsuperscript{138}Id. at 25 (reporting more than eighty percent of all reported appraisal cases involved cash outs and only six arose in transactions among independent corporations when the shareholders had the right to continue as an owner of the changed enterprise).
\textsuperscript{139}\textit{DELAWARE CODE ANN.} tit. 8, § 262 (2001).
\textsuperscript{140}Id. § 262(b).
\textsuperscript{141}Id. § 262(b)(1).
\textsuperscript{142}Id. § 262(b)(2).
\textsuperscript{143}In fact, there were less than a dozen cases a year and some of those were pro se. \textit{See} Thompson & Thomas, supra note 28, at 167 tbl. 1.
same path, therefore, will not produce a fiscal crisis of that sort. The
coming race will be as Mark Roe has said, more horizontal.\textsuperscript{144} The greater
risk is that the number of relevant issues left to state corporate law will be
replaced by the rules of Congress, the SEC, or the stock exchanges. This
decline will be felt by the Wilmington bar in terms of the range of topics
on which its renowned expertise will be sought, by the ten judges who will
make less of American corporate law, and by academics with extensive
knowledge of Delaware corporate law that will now be less useful. This is
the obsolescence that Bayless Manning predicted over forty years ago when
he described corporate law as having rotted away. "We have nothing left
but our great empty corporation statutes—towering skyscrapers of rusted
girders, internally welded together and containing nothing but wind."\textsuperscript{145}
American corporate law passed through that crisis in part because of the
essential wisdom of the Delaware mission statement. A minimalist legal
structure trusting directors, relying on a variety of markets and other checks
on director behavior, permitting directors to pull incentives and monitors
from various places, and using ideas developed by other sources has proved
to be an effective way to run a corporation. If the structure, however, does
not account for the current roles of officers, directors and shareholders and
the current forms in which transactions take place, then other governance
providers will take over Delaware's traditional area of corporate
governance.

\textsuperscript{144}Roe, Delaware's Politics, \textit{supra} note 4.

\textsuperscript{145}Bayless Manning, \textit{The Shareholder Appraisal Remedy: An Essay for Frank Coker},
72 \textit{Yale L.J.} 223, 245 n.37 (1962).