

INTRODUCTION:
THE DELAWARE GENERAL CORPORATION LAW
FOR THE 21ST CENTURY

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To give credit where credit is due, this introduction should begin with reference to an email message I received from Vice Chancellor Leo E. Strine, Jr. in the fall of 2007. In that message the Vice Chancellor graciously asked me to assist him in preparing an issue of the *Delaware Lawyer* on the occasion of the fortieth anniversary of the 1967 revision of the Delaware General Corporation Law.¹ The issue would be called "Folk at 40"—referring to the report prepared by Professor Ernest L. Folk, III for the commission that developed that revision. Recognizing that the *Delaware Lawyer* articles would have to be quite short, the Vice Chancellor suggested that the subject might also be suited to a more expansive academic treatment.

That was the inspiration for the symposium presented at Widener Law School's Delaware campus on May 5, 2008, and the articles published in this issue of the *Journal*. Thus, we include in this issue a fuller version of the fascinating interview with Charles F. Richards, Jr., Charles S. Crompton, Jr., and the Honorable Walter K. Stapleton, who review and reflect on their involvement in the revision effort over forty years ago when they were young associates and assistants to the principal drafters of the revision. Their recollections are an invaluable (and frequently entertaining) addition to the records of the revision project.²

Several of the articles in this issue are expanded versions of the authors' contributions to the *Delaware Lawyer* issue.³ The other contributors to this

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¹*Folk at 40: The Past and Future of the Delaware General Corporation Law*, DEL. LAW., Spring 2008 at 7-36.

²An extensive collection of the documents generated in connection with the 1967 revision, including the report by Professor Folk to the Delaware Corporation Law Revision Committee, is available at [http://law.widener.edu/LawLibrary/Research/Online Resources/DelawareResources/DelawareCorporationLawRevisionCommittee.aspx](http://law.widener.edu/LawLibrary/Research/OnlineResources/DelawareResources/DelawareCorporationLawRevisionCommittee.aspx).

³Frederick H. Alexander, *An Optimal Mix of Clarity and Flexibility*, DEL. LAW., Spring 2008, at 31; R. Franklin Balotti, Donald A. Bussard & Thomas A. Uebler, *The (Mis)Application of Section 144*, DEL. LAW., Spring 2008, at 22; Joel Edan Friedlander, *Overturn Time-Warner Three Different Ways*, DEL. LAW., Spring 2008, at 34; J. Travis Laster, *Goodbye to the Contemporaneous Ownership Requirement*, DEL. LAW., Spring 2008, at 25; Robert B. Thompson, *Folk at 40: Filling the Shareholder Space*, DEL. LAW., Spring 2008, at 26; Edward P. Welch & Robert S. Saunders, *Enabling Delaware's Success*, DEL. LAW., Spring 2008, at 33.

symposium issue were selected in response to a call for papers that invited authors to address possible modifications or improvements to the Delaware General Corporation Law that might make it a more efficient vehicle for business, both in the United States and globally.

In all of these articles, the authors rose nobly to the challenge. Each of the pieces published here is thoughtful and provocative. Some of the proposals put forward are quite narrow in scope, while others are broad, and yet they each articulate a distinct perspective on the role and character of the corporation law.

In this introduction I offer a brief tour of these articles, taking the occasional liberty of adding a personal editorial comment of my own.

By way of overview, we adopt the same thematic breakdown in this issue that we used during the live presentations in May 2008:

- The Delaware General Corporation Law and Takeovers
- Stockholder Litigation Under the Delaware General Corporation Law
- Stockholders in Corporate Governance
- What We Can Learn from Other Statutory Schemes

Needless to say, the boundaries among these categories are hardly impermeable. For example, the articles by Bob Thompson and Brett McDonnell, while in separate categories, both speak to the subjects of takeovers and the role of stockholders in governance. We hope that they and the readers will indulge the somewhat arbitrary separation of these two excellent pieces.

In any event, the first category, addressing the role of the corporation statutes and takeovers, includes the contributions by Joel Friedlander and Brett McDonnell. In his article, Friedlander sees the 1990 opinion of the Delaware Supreme Court in *Paramount Communications, Inc. v. Time Inc.*⁴ as a low water mark in the evolution of sound corporate law, and urges several statutory changes to reverse the failings he perceives in that opinion. In particular, he decries the open-endedness of the directors' legal mandate, urging that the statute direct them in all cases—not just sales of the company—to make shareholder wealth maximization their exclusive goal. Likewise, he advocates clearer statutory authorization for bylaws—including those adopted by stockholders—that would limit the board of directors' ability to adopt and maintain a "poison pill" shareholder rights plan. Third, and most intriguingly

⁴571 A.2d 1140 (Del. 1990).

to me, Friedlander questions the virtually unconstrained discretion of boards of directors of acquirers, and suggests that the statute afford acquirer stockholders a vote on major acquisitions. Friedlander nicely describes the gradual deterioration of acquirer stockholder voting rights through the development of statutes like Delaware's section 251(f),⁵ cash-out mergers, and triangular mergers, and recounts several earlier scholarly proposals to reverse that development. Nevertheless, as Friedlander points out, the undeniable disparity in legal constraints—notably shareholder voting—applicable to bidder and target managements has received remarkably little scholarly attention, and remains a worthy topic for consideration.

Professor McDonnell's article focuses exclusively on the utility of clarifying or expanding the extent to which bylaws—including those adopted by stockholders—can regulate important matters of corporate governance or conduct. McDonnell and I have shared an academic affinity for this issue, although our substantive views are not by any means identical.⁶ Both here and in our earlier writings, moreover, neither of us had the benefit of the guidance offered by the Delaware Supreme Court's landmark opinion in July 2008 in *CA Inc. v. AFSCME Employees Pension Plan*.⁷ That opinion's focus on bylaw power to regulate matters of process certainly seems to lend support to McDonnell's first proposal, *viz.* to clarify stockholder power to adopt bylaws relating to procedural and governance rules, and to preclude bylaws dealing with substantive business decisions.⁸ As I read the *AFSCME* opinion, however, the validity of bylaws limiting the board's ability to adopt poison pills is even more doubtful than before, under existing Delaware law—although McDonnell and others may well disagree, and McDonnell in any event is proposing a legislative prescription that would override any contrary instruction in the *AFSCME* opinion or earlier precedent. McDonnell's third proposal is to establish that stockholders may adopt a bylaw that includes a provision precluding the board of directors from repealing or amending it. Again, he and I disagree about the state of existing Delaware law—I have maintained that such a provision is currently invalid⁹—but McDonnell is

⁵DEL. CODE ANN. tit. 8, §251(f) (2001).

⁶*Compare* Lawrence A. Hamermesh, *Corporate Democracy and Stockholder-Adopted Bylaws: Taking Back the Street?*, 73 TUL. L. REV. 409 (1998) (urging that poison pill-limiting bylaws are contrary to Delaware law), *with* Brett H. McDonnell, *Shareholder Bylaws, Shareholder Nominations, and Poison Pills*, 3 BERK. BUS. L.J. 205 (2005) (urging the opposite position).

⁷953 A.2d 227 (Del. 2008).

⁸*Id.* at 234-35 ("It is well-established Delaware law that a proper function of bylaws is not to mandate how the board should decide specific substantive business decisions, but rather, to define the process and procedures by which those decisions are made.").

⁹Hamermesh, *supra* note 6, at 469-75 (citing *Centaur Partners, IV v. Nat'l Intergroup*,

urging a statutory prescription.

The second category of presentations included in this issue focuses on the statutory rules governing stockholder litigation. In this category we have submissions from Travis Laster, Elizabeth Nowicki, and Blake Rohrbacher, each exploring quite distinct aspects of the general topic.¹⁰ Laster's article is a masterpiece of simplicity and cogency: he says that the statutory requirement of contemporaneous share ownership for standing to sue derivatively lacks any convincing policy foundation. Laster's account of how the requirement became embedded in the Delaware General Corporation Law is a marvelous story of historical accident, damnation with faint praise, and grudging acceptance. It will be interesting to see if anyone, faced with Laster's challenge, rises to defend the requirement as a matter of policy.

Professor Nowicki takes on Delaware General Corporation Law section 102(b)(7), questioning its impact in promoting managerial failures to prevent corporate fraud and other misconduct. Her behavioral premise is plain and plausible, even if debatable: "the threat of punishment is an important motivator of actor behavior." Despite her concern about section 102(b)(7), Nowicki's proposal to amend it is relatively and sensibly modest: eliminate existing limitations on director liability, but establish a cap of liability limited to the greater of improperly received gains or annual director compensation. Nowicki acknowledges that with such a cap, the incentive to bring suits challenging director conduct may be limited, and that the threat of liability may not become credible. Therefore, she suggests that the law afford room to award attorneys' fees that are not dependent on or limited by the size of recovery.

Blake Rohrbacher and his colleagues take aim at an equally controversial statutory target, Delaware General Corporation Law section 144. They bring to the surface a long-simmering debate about the role of that statute, and argue for an amendment to codify a limited role. In their view, section 144 merely "allows the courts to determine whether to analyze an interested transaction exclusively under the common law of breach of fiduciary duty or under both the common law of voidability *and* the common law of breach of fiduciary duty." As they see it, what section 144 does not do is provide a safe harbor definition for application of fiduciary duty principles and

Inc., 582 A.2d 923, 929 (Del. 1990), for the proposition that a bylaw limit on board amendment power is invalid because it conflicts with charter-conferred board power to amend and repeal bylaws).

¹⁰Faith Stevelman's excellent contribution relating to shareholder litigation is still in development, and will appear in a future issue of the *Journal*. See Faith Stevelman, *Regulatory Competition, Choice of Forum, and Delaware's Stake in Corporate Law*, 34 DEL. J. CORP. L. (forthcoming 2009).

the business judgment rule. Their attention to the uncertainty on this point is commendable.

The articles by Bob Thompson and Rick Alexander address the subject of the role of stockholders in corporate governance. Professor Thompson, who can claim a direct student-teacher relationship with Professor Folk, provocatively asserts that Delaware has neglected its role in defining the powers and responsibilities of stockholders and officers. He points out that on key issues—shareholder power to nominate directors, set the agenda for shareholder meetings, and others—Delaware has effectively ceded the debate to federal law, primarily through SEC Rule 14a-8. Perhaps this criticism might be marginally more muted today, following the Delaware Supreme Court's entry into the field in the *AFSCME* opinion, but Thompson's overall point undoubtedly still stands. In short, he encourages the statute to be more outspoken on key questions of corporate law—or its proponents will have to be satisfied to cede the field to Congress and the SEC. This is a most interesting challenge, given the well-recognized conservative tendency in Delaware corporate law to allow evolution more through judicial decisions than through statutory definition.¹¹

I suspect that Rick Alexander would respond to Professor Thompson that Delaware law is more fully defined than Professor Thompson suggests. Alexander focuses on the range of bylaws potentially available to permit stockholders to regulate corporate affairs directly. He summarizes important governance matters (like stockholder power to call special meetings) that, by clear statutory provision, can be regulated by the bylaws. Like Professor McDonnell, on the other hand, and consistent with the apparent import of the *AFSCME* decision, Alexander also argues that bylaws may not prescribe substantive management decisions. Alexander applies these premises to evaluate the power of stockholders to adopt bylaws limiting the adoption and use of poison pills. His conclusion in this regard is a useful counterpoint to the opposing position taken by Professor McDonnell.

The last category of the articles in this issue was, to me, the most conceptually intriguing subject of the symposium. In a world of increasingly tenuous boundaries—geographic and otherwise—it seemed worthwhile to ask some of the symposium participants to consider whether and how the potential

¹¹See, e.g., Lawrence A. Hamermesh, *The Policy Foundations of Delaware Corporate Law*, 106 COLUM. L. REV. 1749, 1776-78 (2006) ("Delaware corporate lawmakers embrace the idea that legal issues that depend for their resolution on complex facts cannot and should not be reduced to black letter codification."); Marcel Kahan & Edward Rock, *Symbiotic Federalism and the Structure of Corporate Law*, 58 VAND. L. REV. 1573, 1611 (2005) (noting a preference for "incremental legislation").

for evolution of Delaware General Corporation Law might be informed by business organization systems in other jurisdictions, or even other business organization forms already existing in Delaware itself.

My colleague Ann Conaway brings to the table her expertise in matters of noncorporate entities. Her article challenges us to consider whether the broad range of contractual flexibility in noncorporate entities—particularly in regard to the articulation of managerial and fiduciary duties—could usefully be imported into the corporate law as well. In effect, she argues, such a result could be achieved indirectly, even now, through a merger into a noncorporate entity, by vote of the board and a majority of the outstanding shares. Why not, she asks, allow corporations to restrict or eliminate fiduciary duties directly, recognizing that the irreducible contractual covenant of good faith and fair dealing will persist nonetheless? Professor Conaway's provocative question forces us to examine the continuing utility of mandatory terms of our corporate law, such as fiduciary duties. Are we prepared to embrace a strong contractarian view of corporate law? Or will we resist permission for "contractual" modifications where they might be applied in entities in which the negotiation usually attendant to the organization of privately held firms is diluted, if not completely absent? And if we do resist, will increasing market resort to noncorporate public entities (such as Blackstone Group) render our resistance academic?

Taking a somewhat opposing tack, Ed Welch and Rob Saunders submit in their article that retention of prominent mandatory features of corporate law—annual election of directors, access to corporate records, and fiduciary duties—establishes a recognizable, valuable "brand," and that the ability to choose alternative business forms actually counsels in favor of keeping those mandatory components intact as part of a predictable "branded" alternative. Welch and Saunders pose the following challenge: "Those who oppose mandatory terms in the DGCL must explain why their proposed DGCL [without mandatory terms] would not be redundant in light of the existing LLC Act and [the Delaware Revised Uniform Limited Partnership Act]." In contrast, Welch and Saunders conclude that preserving the mandatory features of corporate law affords business promoters an efficient signal of adherence to generally understood and acceptable standards of conduct.

Finally, we welcome the comments of Professor Jennifer Hill, a noted and notable student of both Australian and U.S. corporate law. Through the lens of two corporate governance developments—the Australian advent of nonbinding shareholder votes on executive pay, and the circumstances surrounding News Corp.'s reincorporation from Australia to Delaware—Professor Hill diplomatically invites us to examine corporate governance experience under regimes—the U.K. and Australia—having similar legal and market characteristics, and to consider, with care to be sure, whether

convergence toward the U.S. governance model is either entirely predictable or wise. Professor Hill's account is a useful resource for those who might wish to turn to other jurisdictions' experience to guide policy choices here in Delaware.

