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OF THE
STATE OF DELAWARE

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By Email
The Delaware State Bar Association Executive Committee
c/o Mark Vavala

Re: Proposed DGCL Amendments

Dear Members of the Executive Committee:

I write concerning the Corporation Law Council's proposed amendments to the Delaware General Corporation Law (the "Proposal"). I do not write to offer substantive comments. Nor do I purport to write on behalf of anyone but myself. Of the three decisions to which the proposed amendments respond, however, I authored two.[1] As a consequence, multiple people have cited me as a reason for the Proposal and the urgency with which it has been presented. They state, and I paraphrase: "McCormick invited this."

To a very limited degree, that is true. I dropped footnotes in both *Activision* and *Crispo* questioning whether corporate amendments might address some of the problems raised by those factual and legal circumstances.

When I flagged the possibility of legislative review, however, I had Delaware's rich and measured tradition of legislative intervention in mind.[2] Here is what I know about that tradition.

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[1] Those decisions are: *West Palm Beach Firefighters' Pension Fund v. Moelis & Company*, --- A.3d ---, 2024 WL 747180 (Del. Ch. Feb. 23, 2024) (Laster, V.C.); *Sjunde AP-Fonden v. Activision Blizzard, Inc.*, 2024 WL 863290 (Del. Ch. Feb. 29, 2024) (corrected March 19, 2024) (McCormick, C.); and *Crispo v. Musk*, 304 A.3d 567 (Del. Ch. 2023) (McCormick, C.). To understand those decisions, I encourage the Committee to read the decisions themselves.

[2] By "legislative intervention," I refer to legislation introduced in reaction to judicial or social events, typically striking at significant substantive issues or problems. I do not refer to the annual legislative review conducted by the Council to surface and correct more routine matters. The Proposal is not the byproduct of a routine annual review. It is a legislative intervention.

- In 1986, the General Assembly enacted Section 102(b)(7) of the DGCL in response to the Delaware Supreme Court's 1985 decision, *Smith v. Van Gorkom*.[3] In *Van Gorkom*, the Delaware Supreme Court held that the board of Trans Union was grossly negligent and breached its duty of care by approving a merger without substantial inquiry or expert advice. The decision prompted a sharp increase in insurance premiums. The General Assembly responded to this outcry with a limited private ordering solution addressing damages for breach of the duty of care. The Corporation Law Council had numerous meetings on the topic, solicited the views of many persons affected by the decision, proposed amendments, and rejected efforts to more broadly address duty of care claims by allowing for injunctive relief in connection with those breached duties. Despite the uproar immediately following *Van Gorkom*, the Council and the General Assembly did not rush to respond. They worked for a year and four months to study the problem, solicited views on a solution, and gained consensus around a legislative response.

- In 1988, the General Assembly enacted Section 203 of the DGCL. In 1982, the United States Supreme Court ruled that "first generation" anti-takeover laws were unconstitutional.[4] Many believed that this rendered Delaware's original anti-takeover statute, adopted in the 1970s, unconstitutional. It was not until the United States Supreme Court upheld an anti-takeover statute in 1987 in *CTS Corp. v. Dynamics Corp.*, however, that the Council proposed draft legislation.[5] Even then, the legislation was put on hold by the DSBA "because the lawyers were not completely satisfied it should be adopted for Delaware."[6] The DSBA hit the brakes despite pressure from Delaware-chartered companies and threats to leave Delaware.[7] Ultimately, after years of resistance,

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[3] 488 A.2d 858 (Del. 1985).

[4] *See Edgar v. MITE Corp.*, 457 U.S. 624, 645–46 (1982) (finding the Illinois Takeover Act, a first generation anti-takeover act, unconstitutional under the federal Commerce Clause).

[5] 481 U.S. 69, 94 (1987) (holding that Indiana's post-*MITE* anti-takeover statute was constitutional, opening the door for other mimic statutes).

[6] Alexandra Clough, *Delaware Readies Sweeping Takeover Bill*, Inv. Dealers' Digest (Oct. 27, 1987), https://www.law.upenn.edu/live/files/8222-a. I cite to a number of secondary sources in this letter, which I would be more than happy to provide if that would be helpful.

[7] *See id.* ("Sources said pressure from some Delaware-charted companies, including Boeing Co. and Hercules, convinced some members of the group that companies might leave Delaware and incorporate in another state more willing to draft an anti-

Delaware adopted the most measured, "third-wave" anti-takeover statute in the country.[8]

- In 2003, the General Assembly enacted amendments to 10 *Del. C.* § 3114 and 8 *Del. C.* § 220 in response to the Enron and WorldCom scandals. The Enron scandal became public in 2001. The WorldCom scandal became public in 2002. And the United States Congress enacted the Sarbanes-Oxley Act in 2002, imposing new requirements on the officers and directors of publicly traded companies. It was not until June 2003, however, that the General Assembly took action. Then, it was a measured approach, amending Section 3114 to provide jurisdiction over corporate officers and amending Section 220 to make it easier to seek books and records.[9]

- In 2014, the General Assembly adopted legislation concerning fee-shifting bylaws in response to the Delaware Supreme Court's decision in *ATP Tour, Inc. v. Deutscher Tennis Bund*.[10] Initially, the Council rushed forward with a legislative solution, first proposing a version of the amendments just two weeks after the ruling in *ATP Tour*. The General Assembly resisted the push for speed over substance, tabling

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takeover law, rather than suffer for Delaware's hesitation."). In a January 9, 2019, interview, Charles Richards of Richards, Layton & Finger, P.A. recalled the process leading to § 203's enactment: "[I]t proceeded slowly with inquires and people calling and suggesting to various Delaware lawyers that they ought to consider amending the [DGCL] to provide similar protections [to Indiana]. And of course, this created some psychological pressure on those leaders of the bar that were working on the Corporate Council because the thought, of course, was if you don't adopt a proper anti-takeover statute . . . some of these companies may move to their home state or a state with more favorable treatment. So, that caused the Corporate Council to begin to consider the question." Interview with Charles F. Richards, Jr., Richards Layton & Finger P.A., by Edward M. McNally, Morris James LLP, U. of Penn., Inst. For L. & Econ., Del. Oral History Project, in Wilmington, Delaware (January 9, 2009), video available at https://www.youtube.com/watch?v=7M624vitdW4, transcript available at https://www.law.upenn.edu/live/files/9508-section-203-richards-finaljpg.

[8] *See* Peter L. Tracey, *The Delaware Debate on Takeover Legislation: No Small Wonder*, 93 Dick. L. Rev. 339, 365–66 (1989).

[9] *See generally* Lewis S. Black, Jr. & Frederick H. Alexander, *Analysis of the 2003 Amendments to the Delaware General Corporation Law* 7 (2003), https://www.law.upenn.edu/live/files/6782-analysis-2003-amend-del-gen-corp-lawpdf (describing the amendment to Section 3114 as a "response to failures in corporate governance that received widespread publicity in recent years").

[10] 91 A.3d 554 (Del. 2014).

> the amendments and requesting that the Council examine the issues further. The Council then undertook the more careful drafting and review process that led to the final version proposed more than a year later.

As these moments in history reflect,[11] legislative intervention in response to judicial or social developments has occurred relatively infrequently since the modern era of the DGCL. And that is for good reason. As the Council remarked in 2014 in connection with the fee-shifting legislation, "[l]egislation is a relatively blunt tool and not sufficiently flexible to permit case-by-case adjustments to differing situations."[12]

These moments in history also illustrate that the rare instances of legislative intervention have involved a cautious and highly deliberative process that allowed time for countervailing views to inform the policy discussion. The resulting legislation was targeted and, by the time of adoption, uncontroversial.[13]

Moreover, rarely has the Council taken action in response to a judicial decision. As Professors Marcel Kahan and Ed Rock observed in 2005, "in Delaware, legislative overturning of judge-made corporate law is practically unheard of."[14] And where the Council has proposed overturning judge-made law, it has been after a final decision, that is, after the Delaware or United States Supreme Courts have weighed in. The Council has never taken aim at a Chancery decision, much less one in a case that is pending before the trial court.

These are the hallmarks of reasoned legislative intervention in Delaware corporate law.[15] Each are integrity-enhancing and insulate the process from the whims, pressure, and politics of private interests. Each prevent collateral attacks on the rule of law. Each serve as important roadblocks preventing a race to the bottom.

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[11] I had limited time to prepare this letter, so I do not represent that my historical recitation is complete. I do, however, think that the takeaways are accurate.

[12] Delaware Corporation Law Council, *Explanation of Council Legislative Proposal* (March 6, 2015), https://www.law.upenn.edu/live/files/6582-explanation-of-council-legislative-proposal--.

[13] Marcel Kahan & Edward Rock, *Symbiotic Federalism and the Structure of Corporate Law*, 58 Vand. L. Rev. 1573, 1600–01 (2005) (noting: "Even within the Delaware bar, proposed amendments hardly ever generate controversy. One reason is that the Corporation Law Section endeavors to make the necessary compromises to reach a consensus.").

[14] *See generally id.* at 1595.

[15] *See generally id.*

Each ensure Delaware's continued credibility and preeminence in the field of corporate law.

None of the hallmarks of Delaware's tradition are present this year. The Proposal was not the product of a cautious and deliberative process. The Proposal is not targeted in scope or uncontroversial. The Proposal does not address Delaware Supreme Court decisions.

Quite the opposite. The Proposal was the product of a rushed reaction, prepared mere weeks after *Moelis* and *Activision* were issued. The Council pushed out the Proposal to the Section in draft form on Holy Thursday, when many of our colleagues in the bar were preparing for a religious holiday, spring break, and eclipse-themed trips.[16] The court received a copy late the night before. Immediately after the draft was sent to the Section, at least two law firms sent client memos out promoting the amendments to their referral sources and clients. The Proposal has moved forward at a pace that forecloses meaningful deliberation and input from diverse viewpoints. It reflects the broadest set of substantive amendments since the 1960s. It is controversial.[17] It preempts the Delaware Supreme Court's opportunity to act as the final arbiter of Delaware law, striking at two cases still being litigated before the Court of Chancery.

So, why the rush? I have heard two explanations. The first is that the decisions at issue run contrary to market practice. That is a legitimate concern, but one that lacks normative force. The fact that "everyone is doing it" is not a reason to do something. The question is whether everyone is doing the right thing: Is the market acting in a manner that is good for corporate law? The second is the Council's concern that the decisions at issue render Delaware corporation law unpredictable.

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[16] *See The Long Form – Special Edition – April 8, 2024*, The Chancery Daily (Apr. 8, 2024) ("The Chancery Daily notes that on the afternoon of Thursday, March 28, 2024 (just before the start of the three-day Easter holiday weekend), the Council for the Corporation Law Section of the Delaware State Bar Association, which is responsible for proposing amendments to the Delaware General Corporation Law, announced a special meeting of the Corporation Law Section to be held today, on Monday, April 8, to vote on proposed 2024 amendments to the DGCL."); *id.* ("More troubling is the fact that amendments (with substantial substantive impact to fundamental principles of Delaware law) were circulated to members of the Corporation Law Section the afternoon before Easter weekend, for a vote of the Section eleven days later.").

[17] The Proposal passed by a "wide margin" at the April 8, 2024 Section meeting. *See The Long Form – April 10, 2024*, The Chancery Daily (Apr. 11, 2024), That was not a surprise given that Delaware defense firms dominate membership and encouraged attorney attendance. What was unusual is that a healthy number of attorneys appeared to express strong dissent to the Proposal, and a large minority of those present ("20 to 30") voted against it. *Id.*

Reasonable minds can dispute that premise. More importantly, reasonable minds can dispute whether the Proposal achieves the intended purpose of predictability or the opposite.[18]

In my view, reasonable minds should be given the opportunity to debate the normative qualities of market practice and whether the Proposal solves the purported lack of predictability in our law. Optimally, that opportunity would occur before the Executive Committee is forced to vote on the Proposal.

Summing it up, did "McCormick invite this?" No, I did not invite this dramatic departure from Delaware's esteemed tradition. To be sure, the trio of decisions raise important issues for policy makers to consider. A legislative response seems both appropriate and destined. But the perceived crisis this year is no different from those of the past where the Council, DSBA, and General Assembly deployed a careful process. There is no justification for the rushed nature of the Proposal nor the unfair decision now being foisted upon the Executive Committee.

To be clear, I do not impute ill motives to the Council. They are all volunteers trying to do the right thing for Delaware. I do, however, think that the process that they have employed is flawed and that more time would facilitate greater deliberation and, no doubt, a better product. Slowing down his process would allow for people to study (or at least *read*!) the lengthy Proposal and potentially propose alternative solutions.

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[18] *See* Sarath Sanga & Gabriel Rauterberg, *Proposed Amendments to DGCL on Stockholder Contracting Would Create More Problems Than They Purportedly Solve*, Harvard Law School Forum on Corporate Governance, https://corpgov.law.harvard.edu/2024/04/05/proposed-amendments-to-dgcl-on-stockholder-contracting-would-create-more-problems-than-they-purportedly-solve/ (Apr. 5, 2024) (stating the proposed amendments "would replace a century of nuanced if imperfect Delaware jurisprudence with an open-ended statement that enables too much to be taken at face value"); *id.* ("At the present, the law of stockholder contracting is fraught with legal uncertainty. Corporations need guidance, and both the Delaware legislature and the Council of the Corporation Law Section are the right institutions to provide it. The question is not whether corporations can form contracts to alter governance—we know they can. The Amendments, which restate that fact without qualification, would only exacerbate the uncertainty."); Ann Lipton, *What is the value of the corporate form?* Business Law Prof Blog (Mar. 29, 2024), https://lawprofessors.typepad.com/business_law/2024/03/what-is-the-value-of-the-corporate-form.html (noting that shareholder agreements adopted pursuant to the Proposal could contain choice of law and venue provisions that will lead to the inconsistent development of Delaware corporation law).

I applaud the Executive Committee's careful consideration of this issue. I thank you for considering my concerns. I am grateful for the attention that you have given to this communication.

Sincerely,

/s/ Kathaleen St. Jude McCormick

Kathaleen St. Jude McCormick
Chancellor