Analysis of the 1994 Amendments to the Delaware General Corporation Law

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CORPORATION

ANALYSIS OF THE 1994 AMENDMENTS TO THE DELAWARE GENERAL CORPORATION LAW

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INTRODUCTION

The Delaware General Corporation Law was amended in 1994 for the fifth consecutive year. Ten separate bills making changes in twelve sections of the statute were approved by the 137th General Assembly. The changes reflect the continuing need to fine-tune and modernize the statute in light of changes in technology and the needs of business. For example, changes in the manner of executing documents to be filed with the Secretary of State and changes in the media in which such documents are made available to the public represent advances in technology. Changes in the indemnification and dissolution statutes represent a response to a perceived desire for increased accessibility to the Delaware Court of Chancery for the resolution of a number of issues. The changes to the appraisal statute, on the other hand, reflect a growing use in the financial community of depository receipts.

This article describes the changes effected by the 1994 amendments and supplements previous reports published by Prentice Hall Law & Business describing amendments to the Delaware General Corporation Law.[1]

FORMATION

Execution, filing, recording of documents [§ 103].—Section 103 of the General Corporation Law, which governs the execution, filing and recording of documents with the Secretary of State was amended in 1994 in several respects. Perhaps the single change made by the 1994 amendments which will have the greatest effect in practice

1 Arsht and Stapleton: Analysis of the New Delaware Corporation Law; Analysis of the 1967 Amendments to the Delaware Corporation Law; Analysis of the 1969 Amendments to the Delaware Corporation Law; Analysis of the 1970 Amendments to the Delaware Corporation Law; Arsht and Black: Analysis of the 1973 Amendments to the Delaware Corporation Law; Analysis of the 1974 Amendments to the Delaware Corporation Law; Analysis of the 1976 Amendments to the Delaware Corporation Law; Black and Sparks: Analysis of the 1981 Amendments to the Delaware Corporation Law; Analysis of the 1983 Amendments to the Delaware Corporation Law; Analysis of the 1984 Amendments to the Delaware Corporation Law; Analysis of the 1985 Amendments to the Delaware Corporation Law; Analysis of the 1986 Amendments to the Delaware Corporation Law; Analysis of the 1987 Amendments to the Delaare Corporation Law; Analysis of the 1988 Amendments to the Delaware General Corporation Law; Analysis of the 1990 Amendments to the Delaware General Corporation Law; Analysis of the 1991 Amendments to the Delaware General Corporation Law; Analysis of the 1992 Amendments to the Delaware General Corporation Law; Analysis of the 1993 Amendments to the Delaware General Corporation Law (Prentice Hall, Inc., 1967, 1969, 1970, 1973, 1974, 1976, 1981, 1983, 1984, 1985, 1986, 1987, 1988, 1990, 1991, 1992 and 1993, respectively). Copies of these articles are available from Prentice Hall Law & Business, 270 Sylvan Avenue, Englewood Cliffs, NJ 07632, (201) 894-5016.

is the change which validates filings with the Secretary of State bearing the signature of only one corporate officer. Section 103(a) formerly required that documents filed by a corporation with the Secretary of State be executed by the corporation's chairman, vice-chairman, president or vice-president, and that they be attested by the corporation's secretary or assistant secretary. As amended, that section requires only one signature of "any authorized officer of the corporation."

The 1994 amendments revise Section 103(c)(5) to except from the recording requirements imposed by that section short form certificates of dissolution qualifying for treatment under new Section 391(a)(5)(ii). This short form dissolution, which first became available in 1994 by virtue of the enactment of Section 391(a)(5)(ii), is discussed below in connection with that section.

Section 103(f) permits corporations to file certificates of correction in order to correct documents previously filed with the Secretary of State that are inaccurate or were defectively executed. The 1994 amendments allow a corporation to file a corrected instrument that replaces the inaccurate or defective document rather than a certificate of correction. While the corrected document must also specify the inaccuracy or defect being corrected, the availability of this format makes for a simpler and more readily understandable corporate record.

Section 103(h) of the General Corporation Law was added to the statute in 1988 to permit any signature on a document filed with the Secretary of State to be a facsimile. The 1994 amendments further modernize the provisions of the statute relating to the manner in which signatures are affixed to provide that documents can be executed with conformed or electronically transmitted signatures.

REGISTERED OFFICE AND REGISTERED AGENT

Change of registered agent [§ 133].—Section 133 of the General Corporation Law previously required that, if the location of a corporation's registered office in the State of Delaware were changed, a certificate certifying the change be recorded in the office of the recorder of deeds in both the county where the corporation's registered office previously was located and the new county. The 1994 amendments to the General Corporation Law require recording only in the latter county.

Resignation of registered agent [§ 136].—Prior to the 1994 amendments, the registered agent for a Delaware corporation could resign by giving the corporation thirty days written notice of its resignation. The resignation became effective sixty days after a certificate was filed with the Secretary of State attesting to the fact that such notice had been given. The 1994 amendments allow registered agents to resign without sending the required notice upon attesting that previous mailings have been returned undelivered on at least two occasions. In addition, the amendments shorten to thirty days the waiting time before a resignation becomes effective.

DIRECTORS AND OFFICERS

Indemnification of officers, directors, employees and agents [§ 145].—Section 145(d) of the General Corporation Law requires that determinations as to whether a director, officer, employee or agent is entitled to indemnification be made by directors who are not parties to the proceeding in question, by independent legal counsel, or by the corporation's stockholders. The 1994 amendments provide that the determination

may be made by a majority vote of the directors who are not parties to the proceeding, even if those directors constitute less than a quorum of the board.

The 1994 amendments also add a new subsection (k) to Section 145, which vests the Delaware Court of Chancery with exclusive jurisdiction over all actions for indemnification or seeking advancement of litigation expenses brought under Section 145 or any bylaw, agreement or other authority purporting to authorize indemnification. This change has the effect of centering litigation with respect to indemnification in the Court of Chancery. The situation in the past was somewhat anomalous: because indemnification proceedings are almost exclusively actions for money damages, there is no common law jurisdiction in equity. Thus, lawsuits involving issues relating solely to indemnification were frequently litigated in the Delaware Superior Court, even though the Court of Chancery deals with almost all other corporate law matters. The new provision is consistent with a number of other sections of the General Corporation Law that grant exclusive jurisdiction to the Court of Chancery.

In addition, new Section 145(k) gives the Court of Chancery power to determine summarily a corporation's obligation to advance expenses (including attorneys' fees) prior to the final disposition of litigation.

STOCK AND DIVIDENDS

Classes and series of stock [§ 151].—Section 151(a) of the General Corporation Law was amended in 1983 to confirm that the voting powers, designations, preferences, rights and qualifications, limitations or restrictions of a class or series of stock could be made dependent on facts ascertainable outside of the certificate of incorporation as long as the certificate of incorporation "clearly and expressly" defined the manner in which those facts were to operate on the provisions governing the class or series of stock. Since that amendment, practitioners have questioned the scope of the term "facts," focusing in particular on whether the term includes events or decisions that may be within the control of the corporation or its board of directors or officers. The 1994 amendments added a sentence to Section 151(a) specifying that the term "facts" "includes, but is not limited to, the occurrence of any event, including a determination or action by any person or body, including the corporation." This amendment resolves the issue in favor of a reading of the statute to permit incorporating in the terms of a class or series of stock facts which depend upon events or determinations within the control of the corporation or a person or entity affiliated with the corporation, including decisions by its board of directors, its officers or its agents. This resolution of the issue accommodates the growing use of classes or series of stock whose terms are closely tied to unpredictable or fast-changing market conditions or which compete with other instruments in the financial markets. While, in proposing this resolution, the Corporation Law Section of the Delaware Bar Association was not unmindful of the possibility that certain self-made facts could be subject to manipulation, it was thought that any potential for abuse should be held in check by market forces, as well as the equitable powers of the courts. *See, e.g., HB Korenvaes Investments, L.P. v. Marriott Corporation,* C.A. No. 12922 (Del. Ch., July 1, 1993) (provision of certificate of incorporation making determination of board "conclusive" nonetheless subject to considerations of good faith).

MEETINGS, ELECTIONS, VOTING AND NOTICE

Voting trusts and other voting agreements [§ 218].—Section 218(a) was amended in 1994 to make it clear that a voting trust may be established either by a single stockholder acting alone or by two or more stockholders acting together. The Court of Chancery had, in one case, acknowledged that the previous language of Section 218(a) appeared to permit the creation of a voting trust by one stockholder but found that such a trust was not a statutory voting trust because the statute contemplated an association of stockholders. *See Fixman v. Diversified Industries, Inc.*, C.A. No. 4721 (Del. Ch., May 5, 1975).

Other amendments to Section 218 adopted in 1994 eliminated the provisions of the statute that limited to ten year terms the duration of voting trusts and voting agreements, and extensions of such trusts and agreements. The effective date provisions for this amendment are intended to insure that parties who had entered into agreements that extended for longer than ten years prior to the adoption of the amendment would not be subject to its effect. Thus, any voting agreement or voting trust, or any amendment thereto, entered into prior to July 1, 1994 is subject to the ten-year limit unless the trust, agreement or amendment specifically provides that the parties intended to be bound by any changes in the law increasing the permitted duration of such agreement, trust or amendment.

MERGER OR CONSOLIDATION

Merger or consolidation of domestic corporations [§ 251].—Prior to the 1994 amendments, Section 251(c) required that following their approval by stockholders, agreements providing for the merger of two Delaware corporations had to be recorded in the office of the recorder of deeds in the county where the registered office of each constituent corporation was located. The 1994 amendments drop the requirement of recording in the county of the corporation which does not survive the merger.

Appraisal rights [§262].—The 1994 amendments made a number of changes in Section 262 intended to include depositary receipts in the existing "market out" exception to the statutory grant of appraisal rights in connection with mergers or consolidations found in that section. These changes appear in Section 262(a), where a definition of depositary receipt has been added, and in Section 262(b), where a number of references to stock have been broadened to refer also to depositary receipts for stock. The "market out" concept limits the right of stockholders whose shares are listed on a national securities exchange, traded on NASDAQ or held by more than 2,000 stockholders to demand the appraised value of their shares. Shares of stock that are so widely held or publicly traded do not have appraisal rights under Section 262 unless they are required in a merger or consolidation to accept consideration other than shares of stock in the surviving corporation or similarly publicly traded or widely held stock. The amendments extend the market out to holders or recipients of depository receipts representing stock, as well as the stock, itself, wherever the receipts are widely held or publicly traded.

SALE OF ASSETS, DISSOLUTION AND WINDING UP

Notice of claimants; payment [§§ 280-281].—Sections 280 and 281 were adopted in 1987 (along with Section 282) as part of a novel package intended to facilitate the winding up of dissolved Delaware corporations in a way which would quantify, limit

or provide safe harbors to directors and stockholders with respect to claims of creditors and potential creditors. The provisions were amended in 1990 and again in 1994. The 1994 changes were intended to incorporate in the statute the suggestions of practitioners who have had experience with these provisions since their enactment in order to make the statutory scheme more felicitous. Some of the changes were also suggested by the decision in the leading case discussing the provisions to date (*In re RegO Company,* 623 A.2d 92 (Del. Ch. 1992)).

Sections 280 and 281(a) provide a notice and claims procedure that allows a dissolved corporation to give notice of its dissolution to certain claimants and to petition the Court of Chancery for approval of the amount and form of security to be posted for certain unresolved claims. Certain of the amendments to Section 280 provide that claimants who are given notice but do not present a claim to the dissolved corporation or its successor entity in a timely manner, or whose claims are rejected and who do not commence a proceeding in a timely manner, will suffer a bar of such claims. The purpose of these provisions is to require that all known claims be presented to the dissolving corporation in a timely manner.

Section 280(c) provides a procedure by which a dissolved corporation may petition the Court of Chancery for a determination of the amount and form of security that the corporation should post for certain claimants. As originally enacted, Section 280(c) provided that the corporation could petition the court for a determination of the security to be posted for contingent contractual claimants and for certain potential future claimants. The 1994 amendments added a new subsection (now Section 280(c)(1)), which provides for the Court of Chancery to determine the amount and form of security necessary to protect claims that are the subject of a pending action, suit or proceeding. This provision brings such claimants into parity with potential future and contingent contractual claimants.

Sections 280 and 281 were also drafted to provide protection for certain claimants whose claims had not arisen but, based on facts known to the corporation or successor entity, were likely to arise or become known to the corporation or its successor entity. As previously drafted, the protection was limited to claims that would arise "prior to the expiration of applicable statutes of limitation." Courts construing that phrase have applied tolling concepts, thereby extending the potential liability of a dissolved corporation for an indefinite period. In order to strike a balance between the need to protect creditors and the undesirability of tying up assets indefinitely, the 1994 amendments impose a five-year limit on potential claims. The limit may, in the discretion of the Court of Chancery, be extended for a period not to exceed ten years after the date of dissolution.

In addition, Section 281(b), which addresses dissolutions in those situations where the formal notice and claim procedure is not followed, was amended to make it clear that corporations could pay current creditors in full prior to adopting a plan of distribution. Section 281(b) was also amended to provide that the plan of distribution include security for only those potential future claims likely to arise or become known to the corporation within ten years of the date of dissolution.

Finally, a new Section 280(a)(1)(f) was added to provide that the notice required by Section 280(a) include the aggregate amount, on an annual basis, of all distributions made by the corporation to its stockholders for each of the three years prior to the date the corporation dissolved.

FOREIGN CORPORATIONS

Definition; qualification to do business in State; procedure [§ 371].—The 1994 amendments added a sentence to Section 371(c) providing that a foreign corporation may qualify to do business in Delaware as provided for in Section 370, even if its name would conflict with the name used or reserved for use by an existing corporation, limited partnership, limited liability company, registered limited liability partnership or business trust as long as the foreign corporation adopts an assumed name as to which no such conflict exists for use when it is doing business in Delaware.

MISCELLANEOUS PROVISIONS

Taxes and fees payable to the Secretary of State upon filing certificate or other paper [§ 391].—The 1994 amendments provide a short-form method of dissolution for corporations that have no assets and have ceased transacting business. The short form dissolution is intended to encourage such corporations to dissolve formally and to pay their franchise taxes rather than simply to permit their charters to lapse for failure to pay franchise taxes. The procedure is available only to minimum franchise tax payers. The provisions creating this short form dissolution appear in Section 391(a)(5)(ii) by way of amendments which reduce the fee payable upon the filing of a certificate of dissolution to $10 (instead of the $40 fee assessed for certificates of dissolution generally) where the certificate of dissolution certifies that the dissolving corporation has no assets and has ceased doing business, that since its incorporation it has only been required to pay the minimum franchise tax and that it has paid all franchise taxes and other fees due the State. An additional amendment which appears in Section 391(a)(7) relieves corporations using the short form dissolution from paying the $50 fee assessed by the Secretary of State for filing and indexing. An amendment to Section 103(c), discussed above, excepting certificates of dissolution for short form dissolutions from the recording requirements imposed by that section also encourages the use of the short form dissolution procedure.

The 1994 amendments also amend Section 391(c) to provide that the Secretary of State will issue not only photocopies of documents, as have been previously available, but also electronic image copies. This amendment reflects an enhancement to the Secretary of State's corporate information systems. New language is also included in Section 391(c) stating that, notwithstanding Delaware's Freedom of Information Act, the Secretary of State will only issue copies in the format and for the fees provided for in the section.

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