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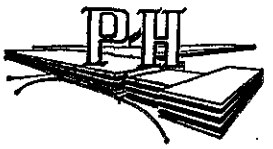

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Analysis of the New Delaware Corporation Law

by

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and

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Members of the Delaware Bar

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ANALYSIS OF THE 1967 DELAWARE CORPORATION LAW

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INTRODUCTION

On December 31, 1963, the Governor of the State of Delaware signed into law an act providing "for a comprehensive review and study of the Corporation Laws of the State of Delaware, and for the preparation of a report containing recommended revisions of such laws." The preamble of the act noted Delaware's leading role as a corporate domicile and declared it to be the public policy of the State "to maintain a favorable business climate and encourage corporations to make Delaware their domicile." It noted also that a number of states had enacted new corporation laws in recent years in an effort to compete with Delaware for corporation business and indicated a legislative desire to maintain and enhance Delaware's position in this area by providing it with a General Corporation Law superior to any then in existence.

The Secretary of State immediately appointed a Committee to carry out this legislative directive. It was comprised of the former Chief Justice of the Supreme Court of Delaware, the Secretary of State, the Director of the State's Corporation Department, two representatives of corporation service organizations, and five leading members of the Delaware Bar having long and varied experience in the corporate field. The committee supplemented its own resources by engaging a research consultant (Professor Ernest L. Folk, III, of the University of North Carolina Law School) and by seeking the counsel and recommendations of more than 100 law firms and corporate legal departments across the country.

Three years of continuous work by the committee, its research consultant and its legal staff produced a comprehensive revision of the prior statute. This proposed new General Corporation Law was introduced in the Delaware Legislature on May 15, 1967. Legislative approval came rapidly, and the new law became effective when it was signed by the Governor on July 3, 1967.

The new statute makes numerous substantive changes in the law. However, it retains the organization and format of the old statute. With very few exceptions, the old section numbers were assigned to the correspond-

ing new provisions, and the former groupings of related sections into subchapters were continued.

The objective of this analysis is to present a synoptic review of the new law in narrative form so that an interested attorney or corporate executive, with a minimum investment of time, may familiarize himself generally with the new law as it relates to stock corporations.[1] This analysis summarizes all of the more important provisions of the law and points out those instances in which the prior law has been significantly changed. In those few instances where the effect of, or reason for, a change is not readily apparent, brief explanatory comments have also been included. The organization of this analysis follows that of the statute in order to facilitate reference to the statute where more detail is desired.

FORMATION

Authority and how to incorporate [§ 101].—Section 101 of the statute grants the authority to incorporate under the General Corporation Law of Delaware to anyone who desires to pursue any lawful business or purposes. The only exceptions are municipal corporations, banks and corporations supported in whole or in part by the State of Delaware.[2] A corporation is formed by and comes into existence upon the filing of a certificate of incorporation with the Secretary of State, unless the certificate specifies a later effective date.

This section differs from its predecessor in that it requires only one incorporator rather than three and authorizes a partnership, association or corporation, as well as a natural person, to organize a corporation [§ 101(a)].

Certificate of incorporation [§ 102].—Section 102 specifies what must and what may be included in the certificate of incorporation. The revision of this section should result in substantially reducing the length of a certificate of incorporation. The certificate must state: the corporation's name, the address of its registered office in Delaware and the name of its registered agent at that address, the nature of its business, the amount and description of the stock it will be authorized to issue, the name and address of the incorporator, and, if the powers of the incorporator are to terminate on the filing of the certificate, the names and addresses of the initial directors.

The portion of the prior statute dealing with the mandatory provisions has been altered in five respects:

First, a corporation's name must now distinguish it from reserved names and names of registered foreign corporations, as well as from the names of domestic corporations [§ 102(a)(1)].

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[1] The new statute, like the old one, applies to non-stock and non-profit as well as stock corporations. In the interest of brevity, however, no attempt has been made here to call attention to those provisions applicable to non-stock and non-profit corporations which differ from those applicable to stock corporations.

[2] Section 1 of Article 9 of the Delaware Constitution of 1897 prohibits the formation of these types of corporations under the General Corporation Law. The reference in the new statute to other laws of Delaware was inserted to indicate that the Delaware statutes should be consulted as well as the Constitution. At present, however, no Delaware statute precludes the use of the General Corporation Law for any purpose other than those which are already precluded by the above cited Constitutional provision.

Second, if it is desired to give the corporation power to engage in every type of business and transaction, this may be accomplished by stating that "the purpose of the corporation is to engage in any lawful act or activity for which corporations may be organized under the General Corporation Law of Delaware," either with or without qualification. This brief statement of the nature of the corporation's business or purposes will probably become a popular substitute for the presently customary several pages of text enumerating the different types of businesses and transactions in which the corporation may engage [§ 102(a)(3)]. The statute also states that it is not necessary to set forth in the certificate of incorporation any of the powers conferred on corporations by the statute [§ 102(c)]. This provision should encourage the draftsmen of certificates to omit the statutory powers which are often included in certificates of incorporation.

Third, the concept of a minimum amount of capital necessary to commence business has been dispensed with through deletion of the old requirement that such an amount, not less than $1,000, be stated in the certificate of incorporation.

Fourth, the requirements that the certificate state whether or not the corporation shall have perpetual existence and whether or not stockholders are to be personally liable for corporate debts have also been eliminated. Instead, perpetual existence and a limitation of each stockholder's liability to any amount remaining unpaid on his stock are the law in the absence of specific provisions in the certificate of incorporation to the contrary [§ 102(b)(5)(6)].

Finally, the initial board of directors may but need not be named in the certificate of incorporation. If they are named, the authority of the incorporators will cease upon the filing of the certificate of incorporation, and the organization of the corporation will be completed by the named directors [§ 102(a)(6)].

Subsection(b) of Section 102, which sets forth the optional provisions which a certificate of incorporation may contain, retains the broad authority to include "any provision for the management of the business and for the conduct of affairs of the corporation, and any provision creating, defining, limiting and regulating the powers of the corporation, the directors and the stockholders, or any class of stockholders," so long as those provisions are not contrary to the laws of Delaware [§ 102(b)(1)]. Two material changes have been made, however, in other portions of this subsection.

With respect to the preemptive rights of stockholders to subscribe to additional issues of stock, the former law recognized the existence of a common law preemptive right but authorized it to be denied or limited by an express provision in the certificate of incorporation. If the certificate was silent on the subject, stockholders had preemptive rights. This was not satisfactory, largely, because there is great uncertainty as to the precise scope of the common law preemptive right. The new law reverses the old law by providing that stockholders shall have preemptive rights only to the extent conferred by the certificate of incorporation. However, the new provision is not applicable to any corporation whose certificate of incorporation, as in effect when the new law became effective, did not contain a provision limiting or denying to its stockholders the preemptive right. Thus, the new statute does not affect anyone's existing preemptive rights and such existing rights, if they are to be changed, must be changed by charter amendment [§ 102(b)(3)].

With respect to the previously existing authorization for requiring a larger vote of stockholders than would be required by the General Corporation Law for corporate action, this authorization has been expanded to permit super-statutory voting requirements for the board of directors as well [§ 102(b)(4)].

Standard provisions for execution, acknowledgement, filing and recording of corporate instruments [§ § 103-106].—Sections 103 through 106 deal with such matters as the execution, acknowledgement, filing and recording of corporate instruments, the evidentiary value of such instruments, and the date upon which the corporate action reflected in such instruments becomes effective.

Prior to the enactment of the new statute, the statutory provisions dealing with incorporation and with major corporate changes each contained its own instructions concerning the procedure for executing, acknowledging, filing and recording the necessary documents. The new statute avoids the duplication and lack of uniformity of that system by establishing a standard procedure applicable to most instances where the execution, acknowledgement, filing or recording of corporate documents is required by the statute [§ 103(a)-(c)].

The other changes reflected in this portion of the statute pertain to the date upon which corporate existence commences and the effective date of major corporate changes. Although the requirement of recording in the office of the Recorder in the county in which the corporation's registered office is located has been reluctantly retained, corporate existence commences and corporate changes now become effective on the date of filing of the requisite instrument with the Secretary of State. They cease to be effective, however, at the expiration of 20 days after the filing date, if the necessary recording is not accomplished within such 20 day period [§ § 103 (d), 106]. This is intended to eliminate the time problem which sometimes arose when a document had to be recorded in a county other than that in which the office of the Secretary of State is located. In addition, the option to make an instrument effective on a future date specified therein, available in some instances under the prior law, is retained and made applicable to certificates of incorporation as well as all other instruments which must be filed and recorded under the statute. The specified effective date under the new statute may be as long as ninety days after the date of filing [§ § 103(d), 106].

Completion of organization of corporation [§ § 107, 108].—Sections 107 and 108 continue to provide the incorporators with the authority to perfect the organization of the corporation and to manage its affairs until they have elected the initial directors. They recognize, however, the new option of naming the initial directors in the certificate of incorporation and authorize any directors so named to adopt the initial by-laws and to otherwise prepare the corporation for the transaction of business. An organization meeting is no longer required, if each incorporator or director signs an instrument stating the action taken [§ 108].

By-laws [§ § 109-110].—The provisions of the statute relating to by-laws were reorganized but not substantively changed. After the initial by-laws are adopted, the power to amend or repeal belongs to the stockholders except to the extent the certificate of incorporation expressly confers that power upon directors [§ 109(a)]. The by-laws may contain any provision "not inconsistent with law or with the certificate of incorporation, relating to the business of the corporation, the conduct of its affairs and its rights or powers or the rights or powers of its stockholders,

directors, officers or employees" [§ 109(b)]. Emergency by-laws, applicable in national emergencies, are also authorized [§ 110].

POWERS

Powers of the corporation [§§ 121-123].—Section 121, like its predecessor, provides that every corporation, in addition to the powers specifically enumerated in the succeeding section, shall have all powers and privileges conferred by law and its certificate of incorporation, together with any powers incidental thereto, to the extent they are necessary or convenient to the pursuit of its business or purposes.

Sections 122 and 123, also like their predecessors, enumerate in very broad terms specific powers which every Delaware corporation shall possess. No power conferred in the previous law has been deleted, although an attempt has been made to clarify the scope of a number of them. Some powers, not previously specified, have been added to the list of specific powers, the most notable of which are the powers to enter into contracts of guaranty or suretyship, to be a partner or joint venturer, to establish pension, profit sharing, stock option and other compensation plans, and to insure the lives of directors, officers, employees and stockholders [§ 122 (11), (13), (15), (16)]. The exercise of each of these powers for the benefit of the corporation and in pursuit of its authorized objectives was generally accepted as proper under prior law, however, and these additions have been made solely for the purpose of clarification.

Effect of lack of corporate power [§ 124].—Section 124 is a new section which, in effect, abolishes the obsolescent, common law doctrine of ultra vires except as applied to (1) a suit by a stockholder to enjoin a corporate action or transfer, (2) a suit by or in the name of the corporation against an officer or director for damages arising from his unauthorized act, or (3) a suit by the Attorney General to dissolve the corporation or to enjoin the transaction of unauthorized business. If a corporation elects to state in its certificate of incorporation, pursuant to Section 102(a)(3), that its purpose is to "engage in any lawful act or activity . . . ," these exceptions will have very limited application.

Denial and qualification of certain powers [§§ 125-126].—Sections 125 and 126 continue the limitation of the previous law on the power to confer academic or honorary degrees and the denial of banking power to any corporation organized under the General Corporation Law.

REGISTERED OFFICE AND REGISTERED AGENT

Registered office and registered agent [§§ 131-136].—Sections 131 through 136 retain the requirement that every corporation maintain an office and an agent in this State. The provisions for a change in the location of that office, and for the change or resignation of that agent are unaltered [§§ 133-136]. Under the prior law, however, the required office was referred to as the "principal office or place of business" and the agent was referred to as the "resident agent." These terms were inappropriate descriptions and have been replaced in the new statute with the terms "registered office" and "registered agent" reflecting the fact that both must be identified in the corporation's certificate of incorporation [§ 102(a)(2)]. Certificates of incorporation and other documents using the old terminology need not be amended, however [§§ 131(b), 132(b)].

DIRECTORS AND OFFICERS

Board of directors [§ 141].—The fundamental principle that the business of a Delaware corporation shall be managed by its board of directors, except to the extent otherwise provided by the statute or its certificate of incorporation, has been retained in the new statute [§ 141]. The rules regarding the size of the board, quorum, the vote necessary for action, committees, staggered terms, action by unanimous consent without a meeting and the other matters set forth in the predecessor of Section 141 have also been unaltered. One feature has been added, however, which may solve a number of practical problems in the operation of committees of a board. Under the new statute, the board may designate one or more directors as alternate members of a committee who may replace an absent or disqualified member at any meeting. This supplements the provision that the committee itself, if the by-laws so provide, may designate a temporary or substitute member [§ 141(c)]. The new statute recognizes that a director may be removed, but does not deal with the causes or procedure for removal [§ 141(b)].

Officers [§ 142].—Section 142 provides for the selection of a president, secretary and treasurer as well as such other officers as may be desired, all of whom shall be chosen as the by-laws direct and hold their offices until their successors are chosen and qualified. It corresponds in substance with its predecessor.

Loans and other assistance to officers and employees [§ 143].—Section 143 authorizes a loan to an officer or employee of the corporation or its subsidiary, a guarantee of his obligation, or any other assistance to him, so long as the directors are of the view that such action may be expected to benefit the corporation. Stock in the corporation may be pledged as collateral for such a loan, although security is necessary only if the directors so require. This authority was also granted by the prior law.

Interested officers and directors [§ 144].—There are numerous Delaware cases involving transactions in which one or more officers or directors of a corporation either were officers and directors of another party to the transaction or had a financial interest in the transaction apart from that of their corporation. The General Corporation Law in the past, however, did not direct itself to these so-called "common" and "interested" officer and director problems. Now, Section 144 establishes statutory guidelines in this area.

Section 144 stipulates that a contract or transaction between the corporation and one of its officers or directors, or between the corporation and another entity in which one of its officers or directors is involved, either financially or as an officer or director, will not be void or voidable, even where that officer or director participates in authorizing the transaction, in any one of the following situations: (1) if the material facts as to both the director's or officer's interest and the transaction itself are disclosed, and those directors having no conflicting interest approve the transaction in good faith by a vote which would be sufficient without counting the vote of any interested director; or (2) if such material facts are disclosed to the stockholders entitled to vote on the transaction and it is approved by those stockholders in good faith; or (3) if the transaction is fair to the corporation at the time it is authorized.

In determining whether a particular transaction comes within the first situation, the votes of interested directors should be disregarded in ascer-

taining the total votes cast, as well as in ascertaining the affirmative votes, so that the requisite director approval will have been given if a majority of the disinterested directors vote in favor of the transaction. The requirement of good faith was inserted in situations (1) and (2) to cover cases where there is literal compliance with the requirement of director or stockholder approval, but some subterfuge has been employed or other impropriety exists. It does not make a determination of fairness necessary to the operation of the first two alternatives. To construe the statute otherwise would, in the light of the third alternative, render the first two alternatives meaningless [§ 144(a)].

Section 144 also reverses existing case law by providing that common and interested directors may be counted in determining the presence of a quorum at a meeting of directors or committee thereof [§ 144(b)].

Indemnification of officers, directors and others [§ 145].—One of the powers specifically conferred upon a corporation under the prior statute was the power to indemnify its officers, directors and certain others against litigation expenses in certain specified instances. [See former Section 122(10)]. Neither the courts nor corporate counsel found the language of this statutory provision wholly satisfactory, however, and numerous charter and by-law provisions were adopted in an attempt to clarify and extend the statutory power of indemnification. The new statute supplements and extends the prior provisions and at the same time establishes limitations on the power to indemnify.

The class of those who may be indemnified by the corporation is expanded to include anyone made, or threatened to be made, a party to a threatened, pending or completed proceeding, whether civil or criminal, administrative or judical, because he is or was a director, officer, employee or agent of the corporation, or is or was serving at the request of the corporation as a director, officer, employee or agent of another corporation, partnership, joint venture, trust or other enterprise [§ 145(a), (b)]. The heirs and estate of such person are also included [§ 145(f)].

The extent of the permissible indemnification depends upon the character of the proceeding. In a suit brought to obtain a judgment in the corporation's favor, whether by the corporation itself or derivatively by a stockholder, the corporation may only indemnify for expenses, including attorney's fees, actually and reasonably incurred in connection with the defense or settlement of the case, and the corporation may not indemnify for amounts paid in satisfaction of a judgment or in settlement of the claim [§ 145(b)]. Where any other type of proceeding is involved, the indemnification may extend to judgments, fines and amounts paid in settlement, as well as to expenses [§ 145(a)].

In no instance can there be indemnification under the statute, unless it appears that the person seeking indemnification has acted in good faith and in a manner he reasonably believed to be in, or not opposed to, the best interests of the corporation [§ 145(a), (b)]. The phrase "or not opposed to" was included to cover the case where a director is engaged in a purely personal transaction, such as a purchase or sale for his own account of stock of the corporation or a purchase of other property, and reasonably believed that the corporation had no interest in the subject matter of his action. Should liability to the corporation be asserted against the director, based on such transaction and the fact that he was a director, he could be indemnified. This would apply, among other situations, where the director is charged with having diverted to himself a corporate opportunity and where he bought and/or sold stock of the corporation.

In addition to this generally applicable standard of conduct, there are additional special limitations applicable to criminal actions and to actions brought by or in the name of the corporation. In a criminal proceeding, the one to be indemnified must have had no reasonable cause to believe that his conduct was unlawful [§ 145(b)]. In a proceeding by or for the corporation, no indemnification may be paid without court approval in respect of any claim, issue or matter as to which the person has been held to be liable for negligence or misconduct in the performance of his duty to the corporation. The Court of Chancery or any other court in which such a suit may be pending is authorized to permit indemnification of expenses incurred in the unsuccessful defense of such suit, however, when, in view of all the circumstances of the case, the person is fairly and reasonably entitled to indemnity [§ 145(b)]. This provision is intended primarily to deal with the case where no bad faith was involved and the type of conduct for which liability was imposed had not been previously determined to be wrongful.

The statute also provides who is to determine for the corporation whether the proposed indemnitee has met the required standard of conduct. This determination is to be made (1) by the directors, by a majority vote of a quorum of disinterested directors, or (2) by independent legal counsel, if such a quorum does not exist or the disinterested directors so direct, or (3) by the stockholders [§ 145(d)].

In addition to authorizing the corporation to indemnify within the specified limits, the new statute also grants to any director, officer, employee or agent of a corporation who has been successful, on the merits or otherwise, in defense of any proceeding or any claim, issue or matter therein, the right to insist upon indemnification from the corporation for the expenses, including attorney's fees, actually and reasonably incurred by him in connection with that portion of his defense which was successful [§ 145(c)].

These basic provisions on indemnification are supplemented by three auxiliary provisions. The first is an authorization for advancing litigation expenses to a director, officer, employee or agent of the corporation upon receipt of an undertaking from him to repay the amount advanced in the event he should ultimately be determined not to be entitled to indemnification [§ 145(c)]. The statute next leaves room for special by-law provisions and contracts by providing that the statutory indemnification shall not be deemed exclusive of any other rights to which those indemnified may be entitled [§ 145(f)]. Finally, the statute empowers a corporation to obtain insurance at its expense to protect anyone who might be indemnified under the statute, including insurance against liabilities which it would be beyond the power of the corporation to indemnify against under the statute [§ 145(g)]. Thus, for example, a corporation may pay premiums on an insurance policy which indemnifies an executive against liability for negligence in the performance of his duty to the corporation. This is simply a recognition of an additional form of compensation which may be provided for an executive in addition to other forms of compensation.

STOCK AND DIVIDENDS

Authority to issue common, preferred and special stock [§ 151].—Section 151 provides the authority for the issuance of stock in one or more classes and in one or more series within a class. It affords great latitude and flexibility in the stock structure of a corporation. The stock issued may be par or no par stock and may have such voting power, dividend

rights, preferences and other rights as are stated in the certificate of incorporation or, when that certificate so permits, in the resolution of the board of directors providing for the issuance of the stock [§ 151(a)]. Preferred stock and special stock may be convertible into other stock of the corporation and may be made subject to redemption [§ 151(b), (e)]. The only significant change in this section of the statute is an addition which makes it clear that a series of stock may differ from every other series of the same class in all respects other than the par value. Thus, series of the same class of stock must all have the same par value or all be no par stock, but, apart from this, there is no requirement of uniformity of rights or restrictions.

Consideration for issuance of stock and required allocation to capital account [§§ 152-154].—The type of consideration which must be received for stock in a Delaware corporation is constitutionally established [Section 2, Article IX, Delaware Constitution of 1897]. Section 152 of the statute, like its predecessor, reflects the constitutional standard by providing that the consideration must consist of cash, labor done, personal property, real property or leases of real property.

The provisions of the prior statute dealing with the amount of the consideration to be received upon the issuance of stock have been reorganized and supplemented in the new statute, but, with two minor exceptions[3], the substantive law in this area has not been altered. Stock may be issued or reissued at such price expressed in dollars, not less than par in the case of previously unissued par value stock, as the directors may fix, or, if so provided in the certificate of incorporation, as the stockholders may fix [§ 153]. The directors' judgment as to the value of any labor and property received remains conclusive in the absence of actual fraud [§ 152].

Similarly, the rules providing for allocation of all or a portion of the consideration received for stock to the corporation's capital account remain basically unchanged. The discretion of the directors on this matter controls, so long as some allocation to capital is made, and the amount allocated to capital for par value stock is not less than its par value. If the directors do not, within the prescribed time, make an allocation to capital, an amount equal to the par value of any par value shares issued and to the consideration received for any no par shares issued is automatically allocated to capital [§ 154].

Definition of surplus [§ 154].—Section 154, like its predecessor, defines surplus as the excess, at any time, of the net assets of the corporation over its capital. "Net assets" was not defined in the old statute. It is now defined as the excess of assets over liabilities. Capital and surplus are not liabilities for this purpose. This conforms with the accepted understanding of these terms under the prior law.

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[3] The new statute changes the prior law by reducing the stockholders vote required to fix the price at which stock may be issued, where the certificate of incorporation reserves that power to them, from two-thirds of the stockholders entitled to vote thereon to a majority. The other change in the substantive law is the abandonment of a distinction between pre-April 1, 1929, corporations and corporations formed after that date. The old law required that the stockholders of pre-1929 corporations were to fix the consideration at which stock would be issued unless the certificate of incorporation otherwise provided. In the case of post-1929 corporations, the directors had the authority to fix the consideration for stock unless the certificate of incorporation conferred that power on the stockholders. The latter rule is now applicable to all corporations.

The draftsmen of the new statute considered and rejected a proposal to adopt and define the concepts of earned surplus, capital surplus and variations of capital surplus. The new statute, like the old, does not in any situation or for any purpose distinguish between earned surplus and capital surplus or other forms of surplus.

Authority to increase capital [§ 154].—Section 154 of the new statute retains the authority previously granted to the directors of any corporation to increase its capital from time to time by adopting a resolution providing that a portion of its surplus be transferred to the capital account.

Fractional shares, scrip and warrants [§ 155].—The new statute expressly sanctions the common practices of paying cash, or issuing scrip or warrants, in lieu of issuing fractional shares. It provides that a corporation may, but is not required to (1) issue fractions of a share, (2) pay in cash the fair value of fractions of a share, or (3) issue scrip or fractional warrants exchangeable for full shares. Scrip and warrants may be issued subject to such conditions as the directors may fix [§ 155].

Partly paid shares [§ 156].—The authority to issue partly paid shares, expressly noted as partly paid and subject to demand for the remainder of the purchase price, remains unchanged. The section has been clarified, however, by a provision that dividends shall be paid on partly paid shares, but only on the basis of the percentage of the consideration actually paid on such shares. The prior version of the statute was susceptible of being construed as permitting payment on partly paid shares of either full dividends, which was the common law rule, or percentage-of-price-paid dividends.

Stock options [§ 157].—Unless otherwise provided in the certificate of incorporation, the directors remain authorized to issue rights, or options on stock, on such terms and conditions as they deem proper. Their judgment as to the consideration for the issuance is conclusive in the absence of actual fraud [§ 157].

Stock certificates [§ 158].—Every stockholder is entitled to a certificate stating the number of shares owned by him in the corporation [§ 158]. This provision has been changed only with respect to the instances where facsimile signatures of corporate officers are permitted. If the stock certificates are manually countersigned, by either an outside transfer agent or registrar, the signatures of the corporate officers may be facsimilies. The countersignatures of the transfer agent or registrar, but not both, may also be facsimilies. The validity of a stock certificate is not affected by the fact that it bears the signature of a person who had ceased to be an officer before it was issued.

Tax free status for stock and other securities held by non-residents [§ 159].—The Delaware Constitution provides that stocks and bonds of a Delaware corporation shall not be subject to tax by the State of Delaware, when owned by non-residents or by foreign corporations [§ 6, Art IX, Delaware Constitution of 1897]. Section 159, like its predecessor, embodies this constitutional policy.

Power of corporation to own and deal with its own stock [§ 160].—Section 160 authorizes a corporation to purchase, hold, sell and otherwise deal in its own stock, provided that purchases may be made only out of surplus. The prior version of this section also provided that shares of stock belonging to the corporation could not be voted "directly or indirectly." This has been deleted in favor of a provision disenfranchising stock held by the cor-

poration, or by a subsidiary in which the corporation owns more than 50 per cent of the stock entitled to elect directors. The new statute also expressly sanctions the voting of stock by the corporation, where such stock is held in a fiduciary capacity.

Issuance of additional stock [§ 161].—Section 161, like its predecessor, authorizes the directors to issue, at any time, additional shares of stock, up to the amount authorized in the corporation's certificate of incorporation.

Stock subscriptions [§ § 165-166].—The statute includes two new sections concerning stock subscriptions. Subscriptions must be in writing and signed by the subscriber or his agent [§ 166]. A pre-incorporation subscription is irrevocable for six months from its date, unless otherwise provided in the subscription, or unless the revocation is consented to by the corporation or by all other subscribers [§ 165].

Liability of stockholders and subscribers on stock not paid in full [§ § 162-164].—A subscriber for stock who has not paid the entire subscription price, and the holder of stock not paid in full, are subject to statutory liabilities, in addition to any liabilities they may otherwise have as a matter of contract law. In the event of the corporation's insolvency, they are liable to creditors in an amount not exceeding that portion of the agreed consideration remaining unpaid [§ 162(a), (b)]. In addition, any holder of stock not paid in full is liable to the corporation for such amount, up to the unpaid portion of the agreed consideration, as the directors determine the business requires [§ § 163, 164]. However, transferees of shares or subscriptions, who took in good faith and without knowledge or notice that the full consideration had not been paid, are not liable for the unpaid balance. The transferors remain liable in such instances [§162(c)].

Since Section 156 requires the corporation to state on each certificate issued for partly paid shares the amount which is to be, and the amount which has been, paid thereon, the transferee of a stock certificate for partly paid shares will have notice of the facts, if the corporation has complied with that section. The statute also stipulates that a pledgor, rather than the pledgee of stock, is to be subject to the statutory liabilities, and that no fiduciary holder of stock shall be personally liable, as distinct from the estate or fiduciary funds, for the unpaid portion of the consideration [§ 162(d)].

The primary change effected in this area of the law was the elimination of a limitation of the liability of holders of partly paid par value stock to "the sum necessary to complete the amount of the par value" of each share. Holders of partly paid par value stock, like the holders of partly paid no par stock, are now liable for the full balance of the agreed price.

Replacement of lost, stolen or destroyed stock certificates [§ § 167-168].—As under the prior law, a corporation is authorized to issue a stock certificate to replace one that has been lost, stolen or destroyed and may require a bond from the stockholder as a prerequisite to doing so [§ 167]. The stockholder is given a judicial remedy in cases where the corporation refuses to so act [§ 168]. The only significant change here is a transfer of jurisdiction over such enforcement actions from the Superior Court to the Court of Chancery.[4]

[4] Delaware has separate courts of law and equity. The Superior Court is the court of general original jurisdiction at law. The Court of Chancery is the court of original equity jurisdiction.

Situs of stock [§ 169].—For all purposes other than taxation, the situs of stock of a Delaware corporation has always been in Delaware. The statute was not changed in this respect [§ 169].

Dividends [§§ 170, 171, 173].—The substantive law with respect to the funds available for the payment of dividends has not been changed. Dividends may be declared by the board of directors out of surplus (assets less liabilities less capital), or, if there is no surplus, out of the net profits for the fiscal year in which the dividend is declared and/or the preceding fiscal year [§ 170(a)]. The term "surplus" has been substituted for the phrase "net assets in excess of capital" in accordance with the definition provided in Section 154. The wording of the clause permitting dividends out of profits where there is no surplus, or so-called "nimble dividends," has also been altered to make it clear that the appropriate fiscal years for applying the rule are not the latest fiscal year for which complete figures are available and the fiscal year preceding it, but rather the fiscal year of declaration and the fiscal year preceding it [§ 170(a)].

The new statute retains the prohibition against paying nimble dividends when capital represented by stock having a preference upon the distribution of assets is impaired. Also, it retains the special provisions for wasting asset corporations and the authority for dividend reserves [§§ 170(a) and (b), 171]. Similarly, the authority to pay dividends in cash, in property or in shares of the corporation's own capital stock has been retained [§ 173].

Liability of directors for unlawful dividend, stock purchase or redemption [§§ 172-174].—Where directors wilfully or negligently declare a dividend in violation of the provisions of the statute, they are jointly and severally liable to the corporation and, in the event of dissolution or insolvency, to creditors to the full amount of the dividend unlawfully paid [§ 174(a)]. This corresponds with the prior law. A similar provision has been added to the new statute, however, covering the situations where the unlawful act is a purchase or redemption of the corporation's own stock. In either of such events, the directors are jointly and severally liable for the full amount unlawfully paid by the corporation [§ 174(a)]. In either situation, a director is protected if he relied in good faith on the books of account of the corporation, or statements prepared by its officers or by independent public accountants [§ 172].

The provisions for a six-year limit on the bringing of enforcement actions and providing a procedure for an absent or dissenting director to exonerate himself from liability have been retained [§ 174(a)]. In addition, the new statute grants to any director who is held liable a right of contribution against his fellow directors [§ 174(b)], and subrogates him to the rights of the corporation against any stockholders who had knowledge of the facts indicating that the transaction was unlawful [§ 174(c)].

STOCK TRANSFERS

Transfer of stock [§ 201].—Subchapter VI of the prior statute, which contained the provisions of the superseded Uniform Stock Transfer Act, has been repealed in its entirety. Instead, a new Section 201 provides a cross reference to Article 8 of Title 5A of the Delaware Code which contains, in slightly altered form, the provisions of the Uniform Commercial Code pertaining to investment securities.

Restrictions on transfer [§ 202].—The sole reference to stock transfer restrictions in the prior statute was a brief statement in old Section 194

that there could be no restrictions on transfer unless noted on the stock certificate. The case law was sparse and that which did exist cast some doubt on the validity of even some of the more common types of restrictions. The new statute remedies this situation.

Four specific types of restrictions on transfer are expressly sanctioned: (1) rights of first refusal granted to the corporation and/or anyone else and exercisable within a reasonable time; (2) restrictions which involve an obligation of the corporation and/or anyone else to purchase the restricted securities; (3) restrictions requiring the approval of the directors, or of the holders of any class of securities, as a prerequisite to transfer; (4) restrictions prohibiting transfer to designated persons or classes of persons, if such designations are not "manifestly unreasonable" [§ 202(c)]. Any other "lawful restriction on transfer" is also authorized [§ 202(e)].

Restrictions may be imposed by the certificate of incorporation, by the by-laws, or by an agreement among security holders or among such holders and the corporation [§ 202(b)]. They must, of course, be noted on the stock certificates for the restricted securities [§ 202(a)]. The authority granted by the statute includes restrictions on the transfer of securities, other than stock, so that convertible debentures and similar securities may be restricted.

MEETINGS, ELECTIONS, VOTING AND NOTICE

Meetings of stockholders; notice [§§ 211, 222, 229, 230].—The prior statute, by implication, required an annual meeting of stockholders to elect directors. It was a general stated meeting of which the by-laws provided a standing notice and at which, absent a contrary by-law provision, any business could be transacted without other notice.

The new statute expressly requires an annual meeting of stockholders to elect directors, but the place, time and date of the annual meeting need no longer be fixed in the by-laws. They may now be fixed "by or in the manner provided in the by-laws" [§ 211(a) and (b)]. Thus, if the by-laws so provide, the date, place and time of the meeting may be fixed by resolution of the directors. A corporation, accordingly, may now meet in a different city each year without constant amendment of its by-laws. Written notice to each stockholder is required [§ 222] and no business other than the election of directors may be transacted which is not referred to in that notice [§ 211(b)]. The provision permitting meetings to be held either in or out of Delaware is unchanged [§ 211(a)].

As in the prior statute, a stockholder is given a remedy in the Court of Chancery to compel the convening of the annual meeting, if it is not held on the date designated therefor, although the corporation is now allowed a thirty-day grace period before the remedy becomes available. If no date has been fixed, the remedy becomes available thirteen months after the last annual meeting [§ 211(c)].

Recognition is given to the power of a board of directors to call special meetings of stockholders [§ 211(d)].

A procedure for giving notice of both annual and special meetings is also stipulated in the new statute [§ 222]. Notice may be given as early as fifty days and as late as ten days before the meeting [§ 222(b)]. The case law rule that no new notice need be given of an adjourned meeting is codified, but limitations are imposed upon this rule. If the time and place of the adjourned meeting are announced at the meeting at which the adjournment is taken, a new notice must be sent only if the adjournment is for more than thirty days, or if a new record date for voting is fixed [§ 222(c)].

As in the prior statute, a written waiver of notice executed by the persons entitled to notice, either before or after the time stated therein for the meeting, is equivalent to notice [§ 229]. Additional language in the new statute specifies that attendance at a meeting will also constitute a waiver of notice, unless the stockholder appears for the express purpose of registering an objection at the beginning of the meeting to the way in which it was called or convened [§ 229]. Notice need not be given to persons with whom communication is unlawful [§ 230].

Record date for determining stockholders [§ 213].—The new statute authorizes the board of directors to fix a record date for the purpose of determining the stockholders entitled to receive notice, to vote, to receive dividends, rights and the like, or to give consent to corporate action [§ 213(a)]. It deletes the provisions of the prior statute authorizing alternatives which involved closing the transfer books or disenfranchising stock.

The record date may now be set as early as 60 days (previously it was 50 days) preceding the meeting or other corporate action [§ 213(a)]. If no record date is fixed by the board, the statute automatically establishes the day preceding the date upon which notice is given as the record date with respect to notice and voting, and the day upon which the pertinent directors' resolution is adopted as the record date with respect to all other matters [§ 213(b)].

Voting and voting rights [§§ 212, 214-217, 221].—As in the past, each stockholder is entitled to one vote for each share of stock held by him, unless otherwise provided in the certificate of incorporation [§ 212(a)]. The certificate may authorize cumulative voting [§ 214]. Each stockholder may exercise his right to vote, or his right to give written consent to corporate action (*infra,* page 336), by proxy. The effectiveness of the proxy is limited to a period of three years from its date, unless it otherwise provides [§ 212(b)].

The new statute both codifies and supplements existing case law that a proxy is revocable, even though it is stated to be irrevocable, if the power to vote the stock represented by the proxy is not coupled with an "interest." A question unanswered by the Delaware case law was whether the interest necessary to support an irrevocable proxy had to be an interest in the stock for which the proxy was given, or whether it was sufficient if the proxy holder had an interest in the corporation. The new statute resolves this question by providing that the requisite interest of the proxy holder may be an interest in the corporation generally and need not be an interest in the stock itself [§ 212(c)]. Thus, a creditor of the corporation may receive an irrevocable proxy from its stockholders, even though he has no interest in the stock covered by the proxy.

The provisions of the old statute that the certificate of incorporation or by-laws may specify the number of shares which will constitute a quorum and the votes that will be necessary for the transaction of business remain unchanged [§ 216].

The statutory rules for determining the person or persons entitled to vote stock in which more than one person has an interest have been expanded. The prior statute spoke only of pledged stock and stock held in a fiduciary capacity [§ 217(a)]. The new statute covers various additional situations in stock stands of record in the names of two or more persons [§ 217(b)].

Voting trusts and voting agreements [§ 218].—The new statute continues the authorization of ten-year voting trusts, where the agreement is filed with the corporation and the stock involved is transferred to the trustee, as trustee, on the books of the corporation [§ 218(a)].

A new subsection has been added, however, which recognizes the validity of an agreement between two or more stockholders, providing that their shares shall be voted in a particular manner, as they may subsequently agree, or as determined in accordance with a specified procedure. Like voting trusts, such agreements may have an initial duration of no more than ten years [§ 218(c)].

Extensions of both voting trusts and voting agreements, however, are authorized by the new statute for additional terms not exceeding ten years each, under stipulated circumstances [§ 218(b), (c)].

Lists of stockholders and stock ledger [§ 219].—The prior statute required that a list of all stockholders entitled to vote be prepared and made available at every meeting for the election of directors, and for ten days prior thereto. This is now required with respect to all meetings of stockholders. An express restriction is added, however, that the list shall be open to the inspection of a stockholder only "for any purpose germane to the meeting" [§ 219(a)]. Unchanged is the provision of the old statute that the wilful neglect or refusal of the directors to produce the list at a meeting for the election of directors renders them ineligible for election to office at that meeting [§ 219(b)].

The new statute also retains the provision that the stock ledger shall be the only evidence as to the persons entitled to vote, or to examine the list of stockholders and the books of the corporation. It adds that the stock ledger shall also dictate the persons entitled to inspect the stock ledger [§ 219(c)].

Stockholders' right to inspection [§ 220].—Under the prior statute, the only reference to the right of stockholders to inspect corporate records was a provision that the original or duplicate stock ledger should be available at its principal office in this state, during usual business hours, for inspection by stockholders. A substantial body of decisional law existed, however, which provided a gloss on this statutory provision and established that additional common law inspection rights were still in effect.

Section 220 of the new statute codifies much of this decisional law. It recognizes the right of any stockholder of record to inspect and copy his corporation's stock ledger, an existing list of its stockholders and its other books and records, so long as the purpose for doing so is proper. "Proper purpose" is defined as a purpose reasonably related to the person's interest as a stockholder [§ 220(a), (b)]. The burden of proof on the issue of purpose is placed upon the corporation when the inspection sought is of the stock ledger or a list of stockholders, and upon the stockholder when the inspection sought is of books and records [§ 220(c)].

In addition to codifying the case law, Section 220 makes two substantive changes in the law. First, the requirement that the original or a duplicate stock ledger be maintained in Delaware is eliminated. Secondly, jurisdiction over the enforcement of stockholders' rights of inspection is transferred from the Superior Court to the Court of Chancery [§ 220(c)].

Voting and other rights of bondholders [§ 221].—As in the prior statute, authority is granted to confer upon holders of bonds or debentures voting rights, inspection rights, or any other rights of stockholders. This author-

ity is extended in the new statute to cover the holders of other corporate obligations [§ 221].

Vacancies and newly created directorships [§ 223].—Like its predecessor, Section 223 authorizes a majority of the directors in office, even if they be less than a quorum, to fill vacancies on the board. In addition, it provides that a sole remaining director may fill such vacancies, and that a stockholder may call, or petition the Court of Chancery to call, a special meeting of stockholders to fill such vacancies whenever there are no directors remaining in office [§ 223].

Modern methods of record keeping [§ 224].—Section 224 is a new section providing express sanction for such current practices as the maintenance of stock ledger information on magnetic tape. It authorizes the use of punch cards, magnetic tape, microphotographs or any other information storage device for record keeping purposes, provided the records kept in this fashion can be converted into legible form within a reasonable time. It requires that they be so converted upon the request of any person entitled to inspect them [§ 224].

Contested elections of directors [§§ 225, 227].—The Court of Chancery retains the power to determine the validity of the election of any director or officer. Its jurisdiction and the prescribed procedure remain unchanged [§ 225]. In such a proceeding, as well as in a proceeding commenced after the failure to hold an annual meeting, the Court of Chancery is given authority to pass upon the right of any person to vote in the election [§ 227].

Relief from stockholder or director deadlock [§ 226].—The only provision in the prior statute pertaining to deadlock situations was an authorization for the Court of Chancery to appoint a receiver for any corporation whose stockholders had failed to elect directors at two successive annual elections, or at any election ordered by the court.

The new statute expands this statutory authority. Section 226 provides that the Court of Chancery may appoint a custodian for a solvent corporation, or a receiver for an insolvent corporation, whenever a stockholder deadlock has resulted in a failure to elect directors, and whenever a deadlock of directors threatens irreparable injury and the stockholders are unable to terminate the deadlock. A custodian or receiver may also be appointed where the business of the corporation has been abandoned and steps to liquidate have not been taken. A custodian's authority, unlike that of a receiver, is to continue the business and not to liquidate it, unless the Court should otherwise direct.

Consent of stockholders in lieu of meeting [§ 228].—Section 228 of the new statute retains the authority for a corporation to dispense with any meeting and vote of stockholders, as required by statute, if all stockholders give their written consent to the proposed corporate action. In addition, however, it authorizes a corporation to insert a provision in its certificate of incorporation permitting any or all corporate action requiring the vote of stockholders to be taken on the basis of the written consent of less than all of the stockholders entitled to vote upon the action. The only conditions are that the percentage of such consents required for approval of the action be not less than that stated in the statute pertaining to the corporate action involved, and that prompt notice must be given to all stockholders of the taking of the action.

Since written consent may be given by proxy under Section 212, publicly held corporations, as well as those whose stock is closely held, may wish to insert such a provision in their certificates of incorporation.

AMENDMENTS OF CERTIFICATE OF INCORPORATION; CHANGES IN CAPITAL AND CAPITAL STOCK

Amendments of certificate of incorporation [§§ 241-242].—With one notable exception, relating to cancellation of accrued dividends (discussed below), the new statute effects no change in the substantive law pertaining to amendments of certificates of incorporation.

Before a corporation has received payment for any of its stock, it may amend its certificate by a majority vote of its incorporators or directors [§ 241]. After that time, both director and stockholder approval is required. The required stockholder vote is a majority of the stock entitled to vote, except in certain stipulated instances in which a class vote is required. Where a class vote is required, as, for example, where an amendment would adversely affect one or more classes of stock, a majority of the stock of each class having a right to vote as a class is required, in addition to a majority of all stock otherwise entitled to vote [§ 242(d)(1), (2)].

Any amendment is permitted so long as (1) the certificate, as amended, would contain only such matters as could properly be inserted in an original certificate of incorporation, and (2) the amendment itself will not reduce the corporation's capital [§ 242(a), (c)]. The latter provision does not mean, however, that the capital may not be contemporaneously reduced by appropriate action under Sections 243 or 244 of the statute.

When an amendment will involve a change or exchange of the outstanding stock or rights of stockholders, it may set forth any mechanics for effecting such change or exchange [§ 242(a)].

In addition to setting forth this basic framework. Section 242 of the new statute adds one provision which codifies a portion of the case law in this area, and another provision which reverses a portion of that case law. It codifies the rule that a provision in a certificate of incorporation requiring a larger affirmative vote of stockholders than that required by statute cannot be amended or repealed, except by such larger affirmative vote [§ 242(d)(4)]. The new statute rejects, however, the decisional rule that a charter amendment may not cancel accrued dividend rights. It includes an express sanction for canceling or otherwise affecting rights to accrued but undeclared dividends [§ 242(a)(4)]. This substantive change reflects a conclusion that the preservation of such rights was not a constitutional necessity, as well as a judgment that this restriction on charter amendments made little sense as a policy matter, in light of the fact that such dividend rights could be eliminated in a merger with a wholly owned subsidiary.

Reacquisition and retirement of preferred or special shares [§ 243].—Section 243, like its predecessor, performs a number of functions. It supplements Sections 151(b) and 160 by providing that preferred or special stock may be redeemed or purchased to a limited extent out of capital, as well as out of surplus [§ 243(a), (b)]. In addition, it authorizes the directors, by resolution, to retire shares redeemed or purchased solely out of surplus [§ 243(a)(3)].

Finally, when preferred or special stock is reacquired in a conversion or exchange, and the amount of capital represented by the reacquired stock exceeds that represented by the stock issued upon the conversion or exchange, Section 243(c) authorizes the directors, by resolution, to reduce capital by any amount up to the amount of such excess.

Shares redeemed or purchased out of capital, shares retired, and shares reacquired by conversion or exchange assume authorized but unissued

share status, unless the certificate of incorporation prohibits their reissue [§ 243(d)].

When the authority granted by Section 243 is utilized, a certificate reflecting the action taken must be filed and recorded, and the capital of the corporation is reduced as of the effective date of that certificate [§ 243 (e)]. If the certificate of incorporation prohibits the reissue of shares acquired in any such transaction, the filing of this certificate also automatically effects a charter amendment reducing the corporation's authorized capital stock [§ 243(f)].

The only innovation in Section 243 is a provision that shares called for redemption cease to be outstanding for voting purposes, as soon as a written notice of redemption is given, and the funds necessary for the redemption are irrevocably set aside [§ 243(i)].

Reduction of capital [§ 244].—Section 244, like Section 243, has been reorganized and restated in an effort to improve its clarity, but it effects no substantive change in the prior law. It lists eight ways in which a corporation, pursuant to a directors' resolution and an affirmative vote of a majority of its voting stock, may reduce its capital. The new section does reduce from three to one the number of times a certificate of reduction of capital must be published.

Composite and restated certificates of incorporation [§§ 245-256].—The prior statute authorized the Secretary of State to prepare and furnish on anyone's request a document, called a composite certificate of incorporation, which contained only such provisions of a corporation's certificate of incorporation as were currently in effect. The authority to supply composite certificates has been retained. A new provision stipulates, however, that they are not to be filed or recorded, unless accompanied by a certificate stating that such filing and recording have been authorized by the board of directors of the corporation. In any event, a composite certificate does not supersede the original documents on file with the Secretary of State for any purpose [§ 246].

In addition to composite certificates, the new statute authorizes "restated certificates of incorporation." This is a new concept in Delaware. While a restated certificate contains the provisions of the certificate of incorporation currently in effect, it is proposed and formally adopted by the corporation and, upon its filing, supersedes all underlying documents [§ 245].

If the restated certificate merely restates and integrates what is currently in effect, it may be adopted by the board of directors without a vote of stockholders. A corporation may, however, adopt a restated certificate of incorporation which not merely restates and integrates but also substantively amends what is currently in effect. When this occurs, the restated certificate must be proposed by the directors and adopted by the stockholders in the manner provided in the section governing charter amendments [§ 245(b)].

MERGER OR CONSOLIDATION

General authority to merge or consolidate [§§ 251, 252, 254-258].—The distinction in the old law between a merger and a consolidation is preserved in the new statute. In a merger, the surviving corporation is one of the constituent corporations, while in a consolidation the resulting corporation is a new corporation formed by the consolidation itself.

The new statute, like its predecessor, authorizes mergers and consolidations of a domestic corporation with one or more domestic corporations, and of one or more domestic corporations with one or more corporations existing under the laws of any other state of the United States. This authority is applicable whether or not one or more of such corporations are non-profit corporations or non-stock corporations. The new statute broadens this authority to include a merger or consolidation of one or more domestic corporations with one or more corporations existing under the laws of a jurisdiction other than one of the United States, so long as the resulting or surviving corporation is a Delaware corporation [§ 252(a)].

The procedure for effecting a merger or consolidation remains basically the same. Each of the constituent corporations enters into an agreement of merger or consolidation which contains the terms, conditions and mechanics of the transaction and certain other required information [e.g., § 251(b)]. With respect to a foreign corporation, the procedure for entering such an agreement and for obtaining stockholder approval, if necessary, is governed by foreign law [§ 252(c)]. With respect to Delaware corporations, the new statute provides that the directors shall approve the agreement by adopting a resolution to that effect [§ 251(b)]. This replaces the requirement that the agreement be signed by a majority of the directors of the corporation. Except in those situations, discussed below, approval of the agreement by two-thirds of the total number of outstanding shares, including both voting and nonvoting shares, is required [§ 251(c)].

The prior statute provided that the agreement should state, among other things, "the manner of converting the shares of each of the constituent corporations into shares or other securities of the corporation resulting from or surviving * * * [the] consolidation or merger." On the basis of this clause, it was possible, though not necessary, to construe the statute as forbidding anything, other than stock or other securities of the surviving or resulting corporation, to be given in exchange for the stock of a constituent corporation whose separate existence would terminate upon the merger or consolidation.

The new statute settles this open question with respect to the most common types of consideration. It authorizes the payment of cash and/or the delivery of securities of a corporation, other than the surviving or resulting corporation, to the stockholders of a constituent corporation in addition to, or in lieu of, a conversion of their shares into securities of the surviving or resulting corporation [e.g., § 251(b)]. Thus, the new statute sanctions, for example, a merger of one corporation with a subsidiary of another corporation where stock of the subsidiary's parent corporation, rather than stock of the surviving corporation, is to be distributed to the stockholders of one of the constituent corporations. The question of whether the statute permits the distribution of property other than cash or securities of the surviving or other corporation, however, remains an open one.

The new statute adds express authorization for a provision in an agreement of merger or consolidation allowing the board of directors of any constituent corporation to abandon the proposed transaction, even after it has been approved by the stockholders of all the corporations involved [e.g., § 251(d)].

The new statute also provides that, in the case of a merger, the certificate of incorporation of the surviving corporation shall automatically be amended to the extent that changes in the certificate of incorporation are set forth in the merger agreement, without separate action under the

amendment section. This is an express recognition of the prior understanding and practice [§ 251(e)].

Elimination of requirement of stockholder vote in minor acquisitions by merger [§ 251(f)].—The statute contains a new provision which dispenses with the necessity of a meeting or vote of the stockholders in many instances where a corporation is acquiring by merger a substantially smaller business. This is analogous to a corporation's purchase of the business and assets of another corporation in consideration for the purchasing corporation's stock, which may be accomplished by resolution of the directors of the purchasing corporation without any vote of its stockholders. The statute provides that no vote of the stockholders of the corporation which is to survive a merger is required, if the merger will not change the shares of any class of that corporation's stock or otherwise amend its certificate of incorporation, and if the agreement calls only for the issuance of previously authorized shares in a number which does not exceed 15 per cent of the shares of the same class outstanding immediately prior to the merger [§ 251(f)].

Merger of parent and subsidiary corporations [§ 253].—The new statute, like the old, provides an optional means of effecting a merger of one corporation with one or more corporations in which it owns at least 90 per cent of each class of stock. In the case of an upstream merger, where the subsidiary or subsidiaries are being merged into the parent, the merger may be accomplished by action of the directors of the parent without a vote of the stockholders of any constituent corporation. Any stock of a subsidiary held by outsiders may be converted into securities of the parent or bought out with cash or other property. In a downstream merger, where the subsidiary is the surviving corporation, there must be approval by a majority of the stock of the parent corporation [§ 253(a)].

Appraisal rights [§§ 253, 262].—With three exceptions, appraisal rights are granted to every stockholder of a merging or consolidating Delaware corporation who objects to the merger or consolidation in a writing filed with the corporation before the stockholder vote, who does not vote in favor of the merger, and who, within 20 days after the corporation has mailed to him notice of the effectiveness of the merger, demands payment of the value of his stock [§ 262]. Where the right to an appraisal exists, neither that right nor the procedure for enforcing it have been substantively changed in the new statute.

The first exception to the appraisal right is a parent-subsidiary merger effected pursuant to Section 253. In these so-called "short form mergers," the stockholders of the parent do not have appraisal rights, and only the holders of the publicly owned stock of the subsidiary may qualify for appraisal of their stock [§ 253(c), (d)].

The second exception is one established for the first time in the new statute. Section 262(k) provides that the appraisal right does not apply to stock which is either registered on a national securities exchange, or held of record by not less than 2,000 shareholders. The term "national securities exchange" means a stock exchange which is registered under the Securities Exchange Act of 1934.

The third exception is also new. It denies the appraisal right to shares of the surviving or acquiring corporation in the situation mentioned above where a substantially smaller business is being acquired, and the vote of the stockholders of the surviving corporation is not required because the

merger does not require the surviving corporation to issue more than 15 per cent of its shares outstanding before the merger [§ 262(k)].

The second and third exceptions do not apply, if the corporation's certificate of incorporation otherwise provides, or if the stock involved is not being converted solely into stock of the corporation surviving or resulting from the merger or consolidation [§ 262(k)]. It has been asked whether the inclusion of the word "solely" in the latter provision [last sentence of Section 262(k)] has the effect of preserving the appraisal right where, as is often the case, fractions of a share will not be issued by the surviving or resulting corporation, but the stockholder entitled to a fraction of a share may have it sold by the corporation for his account or receive in cash the value of the fractional share. It was not the intention of the draftsmen of Section 262(k), nor of the committee which proposed the new statute, to give an appraisal right merely because a stockholder may receive cash in lieu of a fraction of a share. To construe the statute as preserving the appraisal right in the cash for fractional share circumstance would result in the anomalous situation of some stockholders of a class being entitled to an appraisal and other stockholders of the same class not being entitled to an appraisal, depending on the number of shares they owned.

The rationale behind the first and third exceptions to the appraisal right is that the stockholder's economic position in both instances is not being substantially changed by the merger. The principal rationale behind the second exception is that in the circumstances in which it applies a public and presumably active market for the stock will exist and a dissenting stockholder will not be locked into a situation if he prefers to get out. Experience has taught that the appraisal right is, at best, a mixed blessing that should be preserved only for those cases in which there is no public or active market for the shares.

Miscellaneous provisions concerning merger and consolidation [§§ 259-261].—The former provisions of subchapter IX pertaining to the transfer of the property and rights of the constituent corporations to the resulting or surviving corporation [§ 259], to the powers of the surviving or resulting corporation [§§ 259, 260], and to the effect of a merger or consolidation upon pending actions [§ 261] remain unchanged.

SALE OF ASSETS, DISSOLUTION AND WINDING UP

Sale, lease or exchange of assets [§§ 271, 272].—The new statute does not alter the previously existing rule that the board of directors may sell, lease or exchange all or substantially all of the assets of the corporation when authorized by a vote of the majority of the stock having voting power, or by the written consent of the holders of a majority of such stock [§ 271(a)]. The new statute does, however, add a provision, corresponding to that in the merger sections, authorizing the directors to abandon the transaction after the stockholders have approved it without going back to them for further action [§ 271(b)].

Section 272 of the statute settles the frequently asked question whether the phrase "sale, lease or exchange" includes a mortgage or pledge. It does not. Accordingly, except to the extent otherwise provided in the certificate of incorporation, all or substantially all of the corporation's assets may be pledged or mortgaged without stockholder approval.

Dissolution and winding up [§§ 273-284].—As under the prior statute, a corporation can dissolve before beginning its business pursuant to a vote of a majority of the incorporators or directors [§ 274]. In all other instances, a majority of the whole board must adopt a resolution proposing dissolution, and this must receive the affirmative approval of two-thirds of the voting stock of the corporation [§ 275]. The new statute eliminates the requirement that the notice of the stockholders' meeting and the certificate of dissolution be published.

The new statute adds a provision which authorizes the Court of Chancery to dissolve a corporation having two stockholders, each holding fifty per cent of the stock, where they are engaged in the prosecution of a joint venture but are unable to agree upon the desirability of continuing that venture [§ 273].

The provisions of the prior statute dealing with the winding up of the business of the corporation after its dissolution, with one exception, remain unchanged. Authority is added for the Court of Chancery to order that the existence of a dissolved corporation shall continue beyond the three years provided by statute for the winding up of its affairs [§ 278]. That court may appoint a trustee or receiver to supervise the winding up of the corporation [§ 279].

INSOLVENCY; RECEIVERS AND TRUSTEES

Receiverships for insolvent corporations; powers and duties of receivers and trustees [§§ 291-303].—The provisions of subchapter XI of the statute, with one exception, reflect the prior law. They pertain to receiverships for insolvent corporations, as well as to the powers and duties of all trustees and receivers for corporations who have been appointed by the Court of Chancery. A new section has been inserted which provides that the liquidation of an insolvent corporation may be discontinued whenever it is demonstrated that the cause for liquidation no longer exists [§ 301].

RENEWAL, REVIVAL, EXTENSION AND RESTORATION OF CERTIFICATE OF INCORPORATION

Revocation of voluntary dissolution and other matters [§§ 311-314].—The text of subchapter XII, dealing with revocation of voluntary dissolution, revival of a corporation and other similar matters, tracks the text of the corresponding portion of the prior statute, except where modifications were necessary to conform to changes made elsewhere in the statute.

SUITS AGAINST CORPORATIONS, DIRECTORS, OFFICERS OR STOCKHOLDERS

Service of process on corporations and other matters [§§ 321-330].—With two exceptions, subchapter XIII, which sets forth rules applicable in actions against corporations, directors, officers and stockholders, corresponds with the prior statute. The section dealing with service of process on corporations has been amended to provide that service may be made on any officer, any director, or the registered agent [§ 321]. Secondly, the defense of lack of legal organization has been abolished with respect to suits brought by the corporation, as well as with respect to suits brought against the corporation [§ 329].

CLOSE CORPORATIONS; SPECIAL PROVISIONS

Becoming a close corporation [§§ 341-344].—Subchapter XIV of the General Corporation Law is a new subchapter providing special rules applicable only to close corporations. It is designed to free close corporations from the operation of statutory and case law rules, which are desirable with respect to publicly owned corporations, but which may be unduly restrictive when applied to a corporation whose stock is closely held.

To be a close corporation under the new statute, a corporation must have elected that status, and its certificate of incorporation must contain a provision (1) that its stock may be held of record by not more than a specified number of persons, not exceeding thirty, (2) that all classes of stock shall be subject to one or more restrictions on transfer, and (3) that the corporation shall make no "public offering" of any of its stock within the meaning of the Securities Act of 1933 [§ 342].

The election to become a close corporation may be made at the time of the formation of the corporation simply by inserting the required provisions in the certificate of incorporation and indicating in the heading that it is to be a close corporation [§ 343].

A corporation that is not a close corporation may elect to become one by adopting an amendment making the necessary insertions in the certificate of incorporation. Such an amendment must be approved by two-thirds of each class of stock [§ 344].

Section 342, which sets forth the required certificate provisions, also authorizes a provision establishing the qualifications of the persons who will be entitled to hold stock, either by specifying classes of persons who are entitled to be stockholders or by specifying classes of persons who are not entitled to be stockholders.

Voluntary termination of close corporation status [§§ 345, 346].—A close corporation may voluntarily terminate its status as such by adopting an amendment to its certificate of incorporation, approved by two-thirds of the shares of each class of stock, which leaves its certificate in such form that the corporation will not meet the definition of a close corporation [§§ 345, 346(a)]. The certificate of incorporation may require a greater than two-thirds class vote on such an amendment [§ 346(b)].

Right to refuse to make transfers in violation of certificate provisions. [§ 347].—If the required certificate of incorporation provisions, and the provisions, if any, establishing qualifications for stockholders, are conspicuously noted on the stock certificates, the transferee of stock in a transaction which results in a violation of such provisions is conclusively presumed to have had notice of that violation. In any such instance, the corporation may, at its option, refuse to register the transfer [§ 347].

Involuntary termination of close corporation status [§§ 345, 348].—Whenever one of the required certificate provisions is breached, the corporation will cease to be a close corporation unless, within thirty days after the event is disclosed, the corporation files a notice to this effect with the Secretary of State and takes such steps as are necessary to correct the situation [§§ 345, 348(a)]. The Court of Chancery is vested with jurisdiction to assist a close corporation and its stockholders in combating a threatened involuntary termination of its status. At the request of the corporation or any stockholder, the Court may issue any order necessary to prevent the corporation from losing its status as a close corporation or to restore it to that status [§ 348(b)].

Option for corporation where restriction on transfer held invalid [§ 349].—When a restriction on the transfer of a security is found to be invalid, the unenforceability of the restriction may result in a situation completely foreign to any anticipated by the parties. In recognition of this fact, the corporation is given an option in that event, for a period of thirty days after the entry of the judgment, in which to purchase the security involved. The option price is determined by agreement of the parties or, in the absence of agreement, by the Court of Chancery [§ 349].

Sanction for divergence from "corporate norm" [§§ 350, 351, 354].—Arrangements between the principals of close corporations have been stricken down in a number of instances, on the ground that they were inconsistent with the corporate way of doing business. Three sections of the new statute seek to help in this area:

Section 350 provides that a written agreement among stockholders holding a majority of the stock of a close corporation will not be held invalid, as between the parties, on the ground that it restricts or interferes with the discretion of the board of directors. To the extent directors' acts or omissions are dictated by such an agreement, the directors are absolved from liability, and liability, should there be any, is limited to the stockholders who are parties to the agreement.

Section 351 specifically authorizes a provision in the certificate of incorporation providing that the corporation's business shall be managed by the stockholders rather than by a board of directors. Where such a provision is inserted, the stockholders have the same liability as directors, and are deemed to be directors for the purpose of applying the other provisions of the Corporation Law.

Finally, Section 354 provides that no written agreement among stockholders of a close corporation, or any provision in its certificate or by-laws, shall be invalid on the ground that it is an attempt by the parties to treat the corporation as if it were a partnership, or to arrange relations between stockholders and the corporation in a manner that would be appropriate only among partners.

Stockholder's option to dissolve close corporation [§ 355].—Section 355 authorizes a charter provision granting to any stockholder, or to the holders of any specified number or percentage of shares of any class, an option to have the corporation dissolved at will or upon the occurrence of any specified event.

Additional remedies for deadlock [§§ 352, 353].—As previously noted, Section 226 substantially expands the statutory authority of the Court of Chancery to appoint a custodian or receiver for a corporation. That section is, of course, applicable to all corporations. Sections 352 and 353 provide additional authority in this area with respect to close corporations.

Section 352 authorizes the Court of Chancery to appoint a custodian or receiver for a close corporation, when (1) it is being managed by the stockholders, (2) a deadlock threatens irreparable injury, and (3) any remedy provided in the certificate of incorporation or by-laws or in a stockholders agreement has failed.

Under Section 353, one-half of the directors in office, the holders of one-third of all stock entitled to elect directors, or, in a multiple class situation, two-thirds of any class, may petition the Court of Chancery for the appointment of a provisional director who will have all of the rights and powers

of a regularly elected director. If the court finds that the present board is so divided that the corporation's affairs can no longer be conducted to the advantage of stockholders generally, it may appoint such a provisional director to participate in the management of the business and thereby break the deadlock.

The court may also appoint a provisional director in any instance where it could appoint a custodian or receiver under Sections 226 and 352, if it deems this less drastic remedy to be in the best interest of the corporation [§ 352(b)].

Section 352 also empowers the Court of Chancery to appoint a custodian or receiver upon the petition of a stockholder who has a right to require the dissolution of a close corporation under a certificate provision authorized by Section 355.

FOREIGN CORPORATIONS

Registration of foreign corporations and related provisions [§§ 371-384].—Subchapter X requires the registration of a foreign corporation doing business in Delaware and the appointment by it of an agent upon whom process may be served. The text is substantially the same as that of the corresponding portion of the prior statute.

The definition of foreign corporation has been expanded, however, to include corporations organized under a foreign jurisdiction other than a state of the United States; and two new sections have been inserted which impose additional sanctions on non-complying corporations.

The first provides that any corporation doing business in Delaware without registering may not maintain an action in Delaware, but stipulates at the same time that a failure to register shall not impair the validity of any of the corporation's contracts and shall not prevent it from defending any action in Delaware [§ 383].

The second new provision authorizes the Court of Chancery to enjoin any foreign corporation from transacting business in the state without having complied with the applicable provisions of law [§ 384].

MISCELLANEOUS PROVISIONS

Taxes, fees and other miscellaneous matters [§§ 391-398].—No change of significance has been made in the provisions which now comprise subchapter XVI. Taxes and fees are unchanged.

One section takes on new significance, however. Section 393 provides that "all rights, privileges and immunities vested or accrued by or under any laws enacted prior to the adoption or amendment of . . . [the new corporation law], all suits pending, all rights of action conferred and all duties, restrictions, liabilities and penalties imposed or required by laws [heretofore] enacted . . ., shall not be impaired, diminished or affected by this [new law]."