

[Securities Regulation Daily Wrap Up, CORPORATE GOVERNANCE—Del. Ch.: Musk still can't have eye-popping pay package, \(Dec. 4, 2024\)](#)

Securities Regulation Daily Wrap Up

[Click to open document in a browser](#)

By [Mark S. Nelson, J.D.](#)

The Chancery Court said Tesla shareholders' post-trial approval of Musk's pay package fell short for procedural, timeliness, and substantive legal reasons.

A Delaware judge rejected Elon Musk's bid to reinstate the record-setting pay package previously awarded to him by Tesla, Inc. and later denied to him by a court decision earlier this year in which it was held that Musk's compensation violated fiduciary principles and could be rescinded. In this latest opinion, the court rejected Musk's attempt to reinstate the pay package after obtaining post-trial shareholder ratification of it. The court also awarded plaintiffs' counsel a significantly reduced, but still large, fee for the "total victory" that they won at trial (*Tornetta v. Musk*, No. 2018-0408-KSJM (Del. Ch. Dec. 2, 2024)).

Shareholder ratification falls short. The court's lengthy opinion examined Delaware law in depth on four issues, all of which the court said Musk would lose. From the court's perspective, any single issue (or a combination of them) regarding procedure, timeliness, Delaware substantive law principles, and problems with the proxy statement for the shareholder ratification vote would doom Musk's effort to reopen the court's post-trial opinion.

- **Procedure**—Musk's lawyers raised multiple Delaware court rules that allow reconsideration of certain court decisions. The Chancery Court said that the rules have as their purposes maintaining the integrity of the judicial process and ensuring finality. However, the chief problem the court said with Musk's argument about two of the three court rules is that the shareholder ratification vote was being offered as after-the-fact evidence. Delaware's court rules, by contrast, are aimed at protecting the admission of new evidence that was in existence at the time of trial but hidden or not yet known. A third court rule was inapt because the judgment against Musk contained factual findings; most cases reviewed under that rule do not have such findings. Said the court: "At bottom, Defendants seek to introduce a new fact that they created for the purpose of flipping the outcome of the Post-Trial Opinion. Defendants do not cite to a single case where a court has provided such relief under Rule 54(b) or otherwise. And no wonder: Were the court to condone the practice of allowing defeated parties to create new facts for the purpose of revising judgments, lawsuits would become interminable."
- **Timeliness**—The court noted that shareholder ratification is an affirmative defense if it is timely raised. However, the only precedent cited by Musk's lawyers was a case in which the company won, and the court there was not asked to reverse the outcome of a trial. "Defendants raised the Stockholder Vote defense six years after this action was filed, one and a half years after trial, and five months after the Post-Trial Opinion," said the court. "Wherever the outer boundary of non-prejudicial delay lies, Defendants crossed it."
- **Inadequacy of shareholder ratification vote**—The court opened this section of its opinion by noting that a shareholder vote by itself cannot ratify a conflicted-controller transaction. The court characterized Musk's lawyers' arguments as turning on agency law, which the court suggested turned agency law on its head by conflating the status of shareholders and directors; directors are trustees for shareholders, said the court, not agents of shareholder principals as Musk asserted. Under Delaware law, the court said shareholders can approve corporate acts in two situations: (1) where an agent lacked authority ("legal ratification"); and (2) to affirm that a corporate act is consistent with shareholders' interests ("fiduciary ratification"). The post-trial opinion found that the compensation grant to Musk was a

conflicted-controller transaction and, as such, could raise issues of coercion risk (controller retaliation), bypass risks (controller acts unilaterally without the board) and tunneling risks (controller resorts to related-party transactions to extract corporate value). That means the entire fairness standard is the default review standard and the business judgment rule cannot apply absent the *ab initio* commitment by the controller to abide by the *MFW* protections for minority shareholders, which Musk did not pre-commit to do. “If one could comply with *MFW* by submitting a rescinded transaction to a second, later vote, then the ‘up-front precondition’ requirement of *MFW* would have little meaning, and *MFW* would fail to fulfill its central objective,” said the court.

- **Proxy statement issues**—The court further observed that even if the other problems with Musk’s shareholder ratification theory did not bar his pay package, issues with the related proxy statement would have. Specifically, the way in which the company described the ratification vote included errors and false or misleading statements about the potential ratifying effect of the vote.

Plaintiffs’ fees reduced. Lastly, in what may be the most remembered part of the opinion declining to reopen the post-trial findings by the court, the court declined to award the plaintiffs’ counsel their requested 11 percent of more than 29 million vested Tesla shares (a valuation of about \$5.6 billion as of the date of the court’s post-trial opinion). Musk had argued that the plaintiffs should not get more than \$54.5 million (a 4x lodestar and about 1 percent of the plaintiffs’ request).

The court walked through a detailed analysis of numerous modes of calculating plaintiffs’ fees in a successful litigation but rejected many of them because Delaware’s Supreme Court had done so or because they did not make sense in the context of the case against Musk. As a result, the court adopted the grant date fair value (GDFV) standard and then focused on the results prong of the multi-factor *Sugarland* test. The court noted that the plaintiffs won a “total victory” but that the plaintiffs also were not entitled to a windfall that would be many times larger than the largest award ever made in Delaware. The court settled on 15 percent of the GDFV (\$2.3 billion), which yielded an award of \$345 million.

The court elected not to formally resolve a dispute between the plaintiffs and Musk over how that amount would be paid and simply left it up to Musk and Tesla to decide if they want to pay in cash or in freely tradeable Tesla shares. The award also includes the plaintiffs’ expenses and costs.

In a [separate letter decision](#), the court declined to grant individual shareholders standing to object to the fee petition and declined to award those shareholders any fees. “Permitting any stockholder to appear and object where the parties have every incentive to zealously represent their clients’ interests would lead to deeply inefficient proceedings that potentially undermine the parties’ ability to control the litigation,” said the court. The court said it had mulled the shareholders’ concerns and that the main opinion declining to reopen the post-trial opinion finding Musk’s pay package invalid nevertheless produced a result that will inure to the benefit of all Tesla shareholders.

The case is [No. 2018-0408-KSJM](#).

Judge: McCormick, C.

Attorneys: Gregory V. Varallo (Bernstein Litowitz Berger & Grossmann LLP) for Richard J. Tornetta. David E. Ross (Ross Aronstam & Moritz LLP) for Elon Musk, Robyn M. Denholm, Antonio J. Gracias, James Murdoch, Linda Johnson Rice, Brad W. Buss, and Ira Ehrenpreis. Catherine A. Gaul (Ashby & Geddes, P.A.) for Tesla, Inc.

Companies: Tesla, Inc.

LitigationEnforcement: CorporateFinance CorporateGovernance DirectorsOfficers ExecutiveCompensation
FiduciaryDuties InvestorEducation Proxies ShareholderActivismNews DelawareNews