Strategic Perspectives

Delaware Corporate and Commercial Case Law Year in Review—2023

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This top ten list summarizes significant decisions of the Delaware Supreme Court and the Delaware Court of Chancery over the past calendar year. Our criteria for selection are that the decision either meaningfully changed Delaware law or provided clarity or guidance on issues relevant to corporate and commercial transactions or litigation in Delaware. We present the decisions in no particular order. The list does not include every significant decision, but offers practitioners an array of decisions on varied issues likely to affect business transactions or business litigation.

1. *In re McDonald's Corp. Stockholder Derivative Litigation*, 289 A.3d 343 (Del. Ch. Jan. 26, 2023).

The *Caremark* doctrine recognizes the duty of oversight for fiduciaries of Delaware corporations. It has developed over several decades in the context of claims initiated against directors following some significant corporate trauma. The case law left open whether corporate officers, not just directors, owe a duty of oversight, as well as the contours of any such duty. *McDonald's* answered those questions.

The action concerned the events leading to the termination of McDonald's former Executive Vice President and Global Chief People Officer. Stockholders brought derivative claims against the officer alleging that he breached his fiduciary duties by "allowing a corporate culture to develop that condoned sexual harassment and misconduct" and then ignoring red flags regarding the same.[1] The officer moved to dismiss for failure to state a claim, but the Court denied the motion.

Citing the reasoning of *Caremark*, Delaware Supreme Court precedent holding that officers generally owe the same duties as directors, and agent-principal concepts, the Court clarified that corporate officers, and not just directors, owe a duty of oversight under Delaware law. As the Court explained, given their day-to-day and more hands-on involvement, officers are better positioned than directors to identify potential trouble within the scope of their responsibilities. While recognizing officers have the same duty of oversight as directors, the Court made an important distinction. An officer's oversight duty necessarily is more context specific. It should account for each officer's particular areas of responsibility. Reviewing the allegations in this action, the Court found that the plaintiffs adequately pled that the McDonald's officer had consciously ignored red flags within his sphere of responsibility—*e.g.*, reports of harassment to him—and, under the extreme facts alleged, conceivably acted in bad faith.

Key Takeaways: After *McDonald's*, it is reasonable to expect plaintiffs to target non-director officers more frequently in *Caremark* cases. The pre-suit demand-on-the-board requirement for derivative claims, as well as the obligation to plead bad faith, should minimize the risk of officer liability. Still, companies should heed the decision's lessons considering developed *Caremark* precedent in the director context – paying attention to the existence, adequacy, and utilization of internal reporting systems.

2. *Coster v. UIP Companies, Inc.*, 300 A.3d 656 (Del. June 28, 2023).

Delaware common law has several standards of review for board action interfering with the stockholder franchise or director elections. This decision clarifies and harmonizes these standards.

The action involved a control dispute over the UPI Companies following the death of one of its two equal co-owners. The plaintiff—the deceased co-owner's spouse—desired a buy-out of her shares at a price that would have been injurious to the company. To exert leverage, she blocked stockholder action, leaving the company in deadlock. The plaintiff then filed a petition to appoint a custodian for the company. While that action was

1 *In re McDonald's Corp. Stockholder Derivative Litigation*, 289 A.3d 343, 349 (Del. Ch. Jan. 26, 2023).

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pending, the defendants sold shares to a long-serving company employee. The stock sale was part of a succession plan and had the effect of breaking the deadlock between the co-owners and mooting the custodian action. These events led to a flurry of litigation and appeals, with the plaintiff suing to invalidate the stock sale. Following trial, the Court of Chancery ruled that the company's actions, including the stock sale, satisfied the entire fairness standard. Plaintiff appealed and the Delaware Supreme Court remanded, instructing the trial court to review the defendants' actions using the *Schnell* and *Blasius* standards. After the trial court found those two standards also satisfied, plaintiff appealed again.

The Delaware Supreme Court again affirmed. This time, the Supreme Court took the opportunity to clarify how these heightened standards interact, observing that *Schnell* and *Blasius* "have been and can be folded into *Unocal* review to accomplish the same ends—enhanced judicial scrutiny of board action that interferes with a corporate election or a stockholder's voting rights in contests for control."[2] The Supreme Court went on to describe a unified *Unocal* standard for such cases, applied "with sensitivity to the stockholder franchise."[3] The court first should review whether the board faced a threat "to an important corporate interest or to the achievement of a significant corporate benefit."[4] That "threat must be real and not pretextual, and the board's motivations must be proper and not selfish or disloyal."[5] The court next should review whether the board's response to the threat "was reasonable in relation to the threat posed and was not preclusive or coercive to the stockholder franchise."[6] A properly motivated board that has identified a legitimate threat "must tailor its response to only what is necessary to counter the threat" and its response "cannot deprive the stockholders of a vote or coerce the stockholders to vote a particular way."[7] Applying this standard to the case before it, the Supreme Court found no error in the Court of Chancery's judgment.

Key Takeaways: *Coster* sets forth a unified *Unocal* analysis where board action interferes with a corporate election or a stockholder's voting rights in contests for control.

3. *Simeone v. The Walt Disney Co.*, 302 A.3d 956 (Del. Ch. June 27, 2023).

Today's heated political climate has given rise to many lawsuits, including in Delaware. While the facts were newsworthy, this Court of Chancery decision reinforced long-standing Delaware law that affords deference to a board's unconflicted business decisions.

Here, a stockholder sought books and records related to the Disney board's decision to criticize Florida House Bill 1557, titled the "Parental Rights in Education" bill, what commentators have characterized the "Don't Say Gay" bill. After Disney constituents demanded that the company publicly oppose the bill, and the company did so, Florida's legislature voted to dissolve the special tax district that housed Disney's Orlando resort. The stockholder alleged mismanagement by the board and sought records to investigate that claim. The company voluntarily provided limited records, but the stockholder sued to obtain more.

The Court of Chancery denied the additional inspection request for multiple reasons. Most notably, the Court held that the plaintiff did not allege a credible basis to suspect wrongdoing by Disney's board. As the Court explained, the board was unconflicted and the directors' decision to speak on a public policy issue fell within their business judgment. The board actively deliberated a response to the bill, and it was consistent with the directors' exercise of their fiduciary duties to consider how the company's public stance would affect its employee and creative partner relationships. Disagreement with a board's business judgment, even when that decision-making leads to negative consequences, does not entitle a stockholder to inspect books and records. The Court thus applied and reinforced long-standing Delaware law that defers to unconflicted boards.

Key Takeaway: The opinion should ameliorate any concern that Delaware courts might second-guess a board's thoughtful business judgment regarding a public policy matter.

4. *In re Edgio, Inc. Stockholders Litigation*, 2023 WL 3167648 (Del. Ch. May 1, 2023).

The *Corwin* doctrine generally insulates from fiduciary duty claims—*i.e.*,

2 *Coster v. UIP Companies, Inc.*, 300 A.3d 656, 672 (Del. June 28, 2023).
3 *Id.* at 673.
4 *Id.* at 672.
5 *Id.*
6 *Id.* at 672–73.
7 *Id.* at 673.

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"cleanses"—non-controlling stockholder transactions that are approved by the fully informed, uncoerced vote of disinterested stockholders. This decision recognizes a limit to *Corwin* cleansing regarding defensive measures and claims under *Unocal*.

The action concerned a transaction by which Limelight Network acquired a business unit of a third party in exchange for a 35% equity interest in Limelight. In that deal, the parties executed a stockholder agreement that: (1) required the third party vote its 35% interest in favor of the board's recommendations (including nominees); (2) gave the third-party nomination rights for director seats on Limelight's board; (3) prohibited the third party from transferring its shares for two years generally, and for three years to certain enumerated parties (competitors of Limelight and any activist investor appearing on specific list); and (4) included a standstill period. Limelight disclosed the arrangement in the proxy and the stockholders approved the transaction.

Stockholder-plaintiffs brought claims to enjoin all elements of the stockholder agreement other than the standstill. The plaintiffs argued that Limelight's board violated its fiduciary duties under *Unocal* because the agreement had the effect of entrenching the directors. Limelight moved to dismiss the complaint arguing that, because of the fully-informed stockholder vote approving the transaction, *Corwin* applied and cleansed the transaction, invoking the business judgment rule.

The Court of Chancery denied the motion, finding *Corwin* inapplicable. The Court reasoned that cleansing *Unocal* claims for injunctive relief would not serve *Corwin*'s "underlying policy rationale of allowing stockholders to make free and informed choices based on the economic merits of a transaction."[8] Unlike *Corwin*, which arose to restrict post-closing claims for money damages in transactions approved by stockholders, *Unocal*'s "core function is … providing a framework for evaluating whether an injunction should issue against defensive measures."[9] Here, because plaintiffs had adequately pled that the board instituted a defensive measure against the perceived threat of activist investors, the complaint triggered *Unocal* review and stated a claim for injunctive relief that *Corwin* could not cleanse.

Key Takeaway: Under *Edgio*, *Corwin* cleansing has its limits—it does not reach claims under *Unocal* seeking injunctive relief.

5. *Colon v. Bumble, Inc.*, 305 A.3d 352 (Del. Ch. Sep. 12, 2023).

As this decision illustrates, the Delaware General Corporation Law (the "DGCL") provides considerable flexibility for corporate governance structures. Here, the Court found valid a unique charter provision that provided different voting power for a single class of stock based on the identity of the stockholder.

The decision concerned the corporate governance structure of Bumble. Bumble's certificate of incorporation provided for one class of stock, with each share carrying one vote, unless it was held by a "Principal Stockholder", in which case each share carried ten votes. A stockholder challenged these provisions as violating Delaware law.

The Court of Chancery granted summary judgment in the company's favor, finding the provisions DGCL-compliant. In reaching this conclusion, the Court reasoned that "nothing in Section 102(a)(4), 151(a), or 212(a) [of the DGCL] requires that the charter frame the voting power appurtenant to a share in terms of a specific number of votes per share."[10] In fact, "Section 151(a) permits special attributes, including voting rights, to depend on facts ascertainable outside of the certificate of incorporation."[11] According to the Court, that is what the parties implemented here. The Court also analyzed Delaware precedent addressing voting rights provisions in similar contexts. Under those authorities, analogous provisions providing formulas for determine voting rights were DGCL-compliant. Thus, Bumble's provisions, carrying the same hallmarks, were valid.

Key Takeaways: *Bumble* gives transactional practitioners additional insight into how the Court of Chancery analyzes provisions affecting stockholder voting rights. Some caution may be warranted—as the Court noted, the action's technical challenge did not provide an opportunity to express "any view on situations in which a governance structure that used identity-based voting could be inequitable."[12]

6. *Cygnus Opportunity Fund, LLC v. Washington Prime Group, LLC*, 302 A.3d 430 (Del. Ch. Aug. 9, 2023).

This decision addresses the duty of disclosure as applied to officers, as well as

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8 *In re Edgio, Inc. Stockholders Litigation*, 2023 WL 3167648, at *1 (Del. Ch. May 1, 2023).
9 *Id.* at *9.
10 *Colon v. Bumble, Inc.*, 305 A.3d 352, 362 (Del. Ch. Sep. 12, 2023).
11 *Id.*
12 *Id.* at 372.

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that duty's application to situations where stockholders had no vote or investment decision to make.

The action involved a squeeze-out merger whereby the controller of a Delaware LLC initially issued a tender offer to buy out the minority investors. After the tender closed, the controller effectuated the squeeze-out merger and the additional minority investors were informed that their membership units had been converted into the right to receive cash. In connection with the merger, the investors received an information statement short on detail. The minority investors sued the company, its board of managers, its controller, and its officers for alleged disclosure violations and other claims. The defendants moved to dismiss.

The Court of Chancery dismissed the fiduciary duty claims against the board and the controller due to the unambiguous waiver of fiduciary duties in the LLC agreement. The officers, however, were not included in the agreement's waiver, and plaintiffs adequately pled claims as to them. For the tender offer aspect of the complaint, the officers argued that they owed no duty of disclosure in that context, and said nothing, so could not have taken on the duty to speak candidly and completely. But the Court found it conceivable that fiduciaries might owe a duty to respond to a severely underpriced tender offer, and may breach that duty by, as here, saying nothing to the investors. As the Court reasoned, "Delaware courts … have not held that directors never have any obligation to speak in response to a tender offer" and "[s]uch a position would be extreme, because directors have an affirmative obligation to respond to threats to the corporation and its stockholders."[13] Here, discovery would need to illuminate whether the board had directed the company's non-disclosure, and whether the officers had reason to believe that following any such direction would be a breach of duty.

Similarly, for the squeeze-out merger aspect of the complaint, the Court found it conceivable that fiduciaries would owe a duty of disclosure in connection with a transaction through which the fiduciaries unilaterally eliminated investors. As the Court declared, it was "not prepared to rule as a matter of law that a fiduciary can take the property of its beneficiary without some level of disclosure, even in the absence of any request for action."[14] Here, the information statement may have breached the duty of disclosure in its incompleteness and misleading nature. Finally, the defendant officers—the CEO, CFO, and the Vice President of Finance and Chief Accounting Officer, respectively—each either signed the information statement or a disclosure violation fell within his or her area of responsibility. Thus, the officer claims survived dismissal.

Key Takeaways: *Cygnus* raises important questions about when tender offers, squeeze-out transactions, or other extraordinary events may give rise to a disclosure duty. It also serves as a reminder of the potential pitfalls for officers with areas of responsibility relevant to corporate disclosures.

7. *Hyde Park Venture Partners Fund III v. FairXchange*, 292 A.3d 178 (Del. Ch. Mar. 9, 2023).

Boards of Delaware corporations frequently include representatives of investors. Delaware law generally entitles those representatives, in their capacity as directors, to the privileged legal advice the company receives. That is because, under Delaware law, each member of the board is considered a joint client within the circle of confidentiality. This decision addresses when an affiliated investor may be entitled to defeat a company's claims of privilege over legal advice received during its designee's tenure.

The action involved a director designee of investment funds who disagreed with his fellow board members about a proposed merger, after which his fellow directors arranged to have stockholders remove him from the board. The investment funds later brought an appraisal action relating to the merger. In discovery, the funds requested privileged communications during the period their designee held office. The company resisted production and the plaintiff moved to compel.

The Court of Chancery granted the motion. As the Court explained, whether the company could successfully assert privilege against the funds turned on whether the company had a "reasonable expectation of confidentiality" as to the director and the funds while the director served.[15] According to the Court, the company had no such expectation in the circumstances. Under settled Delaware law, until there was actual adversity, a committee excluding the director, or an agreement to the contrary, the director was a joint client of privileged information at the company. At the same time, the director was a partner with, and managed, the relevant investment funds. Naturally, he could not avoid sharing information with the funds, because he "(like all humans) has only one brain" and "drew on a unitary store of knowledge when carrying out his dual roles

13 *Cygnus Opportunity Fund, LLC v. Washington Prime Group, LLC*, 302 A.3d 430, 448 (Del. Ch. Aug. 9, 2023).
14 *Id.* at 449.
15 *Hyde Park Venture Partners Fund III v. FairXchange*, 292 A.3d 178, 184 (Del. Ch. Mar. 9, 2023).

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as corporate director and fund manager."[16] In such circumstances, the affiliated investor "presumptively joins the director within the circle of confidentiality."[17] And when joint clients sue each other, one cannot claim privilege against the other for communications during the joint representation. Accordingly, the company could not assert the privilege over the requested materials in discovery.

Key Takeaways: *Hyde Park* provides important guidance regarding company privilege and director designees. As the opinion notes, while investor-affiliated directors may use and share information consistent with the Court's ruling, they do so "at their own risk," as they may face fiduciary liability "if they use the information or permit it to be used for an improper purpose."[18]

8. *Anderson v. Magellan Health, Inc.*, 298 A.3d 734 (Del. Ch. July 6, 2023).

Stockholder M&A lawsuits alleging disclosure violations often are mutually settled or unilaterally mooted by the corporate defendant issuing supplemental disclosures. In either case, the stockholder will seek a fee award for causing the disclosures. This is an aspect of the M&A litigation process constituting the so-called "merger tax." This decision represents another step in Delaware's effort to rein in reflexive and weak M&A suits.

The dispute concerned a stockholder-plaintiff's attempt to enjoin a merger between Magellan Health and Centene Corporation. The plaintiff took issue with certain "don't-ask-don't-waive" standstill provisions and the deal's disclosures. After the company mooted those issues by waiving some standstills and issuing supplemental disclosures, the plaintiff sought a $1.1 million fee award. Magellan opposed the award, arguing for a 90% reduction.

The Court of Chancery sided with Magellan and entered a meager award of $75,000. The Court assigned no value to the standstill waiver. Analyzing the supplemental disclosures, the Court found that they provided modest benefits under the standard announced in *Xoom*, which warrants a fee award when additional disclosures are "helpful." The Court, however, took the opportunity to discuss the evolution of Delaware law's treatment of disclosure-only settlements, including *Trulia*, which in 2016 adopted a standard for disclosure-only settlements requiring the new disclosures to be "plainly material." In the Court's view, *Xoom*'s "helpful" disclosure standard encouraged meritless claims. Seeing room for improvement, the Court announced a new standard for evaluating voluntary supplemental disclosures and mootness fee awards. Going forward, a mootness fee would be earned only if the disclosures were material.

Key Takeaways: Practitioners should be aware of *Magellan*'s materiality standard when assessing potential voluntary supplemental disclosures.

9. *New Enterprise Associates 14, L.P., et al v. Rich, et al.*, 295 A.3d 520 (Del. Ch. May 2, 2023).

Here, a covenant not to sue forced the Court of Chancery to grapple "with a conflict between two elemental forces of Delaware corporate law: private ordering and fiduciary accountability."[19]

The plaintiffs were venture capital funds and early-stage investors in a cloud-based infrastructure company. When the company needed more capital, a new investor joined through a recapitalization. The parties executed a voting agreement in connection with that transaction. The agreement included a drag-along provision that required the parties to approve a sale transaction satisfying certain conditions, as well as a covenant not to sue over the sale transaction. After the deal closed, the new investor effectively controlled the company and its board. Soon thereafter, the company found a buyer and a merger ensued. After the merger, the venture capital funds learned of certain preferred stock issuances and stock options granted to affiliates under the new investor's watch. The funds sued for breach of fiduciary duty regarding the drag-along sale's failing to value claims relating to this conduct. Defendants moved to dismiss, arguing that the drag-along provision and its covenant not to sue contractually barred the plaintiffs' suit.

The Court of Chancery held that the provision was not facially invalid and could be enforced. The Court rejected the "absolutist proposition" that parties can never waive the fiduciary duty of loyalty.[20] The Court's reasoning compared permissive fiduciary tailoring in analogous relationships, such as trusts, agency law, and alternative entities, before discussing corporate fiduciary tailoring in the forms of duty of care exculpation in Section 102(b)

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16 *Id.* at 183.
17 *Id.* at 184.
18 *Id.*
19 *New Enterprise Associates 14, L.P., et al v. Rich, et al.*, 295 A.3d 520, 528 (Del. Ch. May 2, 2023).
20 *Id.* at 540.

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(7) of the DGCL, corporate opportunity waivers in Section 122(17), limited corporate purpose clauses in Section 102(a)(3), statutory close corporation provisions, and other examples. Also relevant was the contractual preemption of fiduciary claims in cases where duplicative contract and fiduciary claims arise out of the same facts. The Court emphasized the contractarian nature of Delaware law, whereunder courts generally respect and enforce voluntary private ordering among sophisticated parties, as well as the DGCL's celebrated flexibility. These concepts, according to the Court, made it difficult to find that the covenant violated publicly policy and was facially invalid.

The Court also considered important the covenant's presence in a stockholders' agreement, rather than the company's charter or bylaws. In that form, the covenant was binding only on the signatories and governed how they could exercise their personal rights, similar to how stockholders may restrict voting or transfer rights in stockholder-level agreements. The Court examined but rejected various other reasoned arguments for invalidating the covenant. The Court agreed that "[a] strong argument exists that a broad, unspecified [fiduciary duty] waiver is facially invalid, such as a covenant not to assert any claims for breach of fiduciary duty under any facts."[21] But the Court distinguished the covenant here as "narrow and targeted." Relying on analogous authorities, the Court set forth a two-step analysis for such covenants. First, the covenant must have sufficient specificity regarding the covered transaction that otherwise could support a fiduciary duty claim. Second, the covenant must be reasonable, assessed by the non-exclusive factors of "(i) a written contract formed through actual consent, (ii) a clear provision, (iii) knowledgeable stockholders who understood the provision's implications, (iv) the [stockholders'] ability to reject the provision, and (v) the presence of bargained-for consideration."[22] Here, the covenant passed muster.

This conclusion, however, did not entitle the defendants to a dismissal of the action. According to the Court, the at-issue covenant reached too far in purporting to restrict "tort liability for intentional harm," in contravention of Delaware law and public policy governing commercial contracts.[23] Here, the covenant's plain language would cover a claim for an intentional, bad faith breach of fiduciary duty in connection with the drag-along sale. The Court declined to enforce the restriction to cover that aspect of the plaintiffs' complaint as a matter of public policy.

Key Takeaways: Delaware law permits a degree of fiduciary tailoring in the corporate context and, as *New Enterprises* holds, under the right set of circumstances that may encompass covenanting to not bring certain fiduciary duty claims.

10. *In re Straight Path Communications Inc. Consolidated Stockholder Litigation*, 2023 WL 6399095 (Del. Ch. Oct. 3, 2023).

Triggering Delaware's entire fairness review in stockholder litigation was once considered outcome determinative and its application greatly incentivized early-stage settlements. That view has waned over time, as defendants have found ways to satisfy the standard's unified fair process and fair price components. This decision is paradigmatic of the trend—the defendants avoided meaningful liability by focusing on the fairness of the transaction's price.

This action concerned breach of fiduciary claims brought against the controller and controlling principal of Straight Path—a publicly held company that spun off from IDT Corporation, both of which were controlled by the same individual. After an FCC investigation revealed certain improprieties associated with assets that IDT transferred to Straight Path in the spin-off transaction, Straight Path's board created a special committee to market the company. The special committee recognized the potential value of an indemnification claim against IDT for its pre-spin-off conduct, which approached $300 million, and sought to carve it out of any sale for the stockholders' benefit. The controller, however, opposed the committee's proposal, injected himself into the process, engaged in a "campaign of abuse and coercion," and threatened to remove any directors opposing him.[24] Ultimately, Straight Path capitulated and agreed to settle the indemnification claim against IDT for $10 million. Shortly thereafter, Straight Path was sold for $3.1 billion, and several stockholders brought claims for breach of fiduciary duty against the controller and IDT.

Defendants bore the burden of establishing entire fairness, measured by a fair process and fair price. The Court of Chancery first held that the controller's overbearing conduct rendered the process unfair. Yet, the settlement's price was within the range of fairness. As the Court explained, Straight Path's indemnification claim essentially

21 *Id.* at 586.
22 *Id.* at 589–90.
23 *Id.* at 593.
24 *In re Straight Path Communications Inc. Consolidated Stockholder Litigation*, 2023 WL 6399095, at *18 (Del. Ch. Oct. 3, 2023).

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was "economically worthless" because the company had failed to provide the contractually required notice to IDT, which had materially prejudiced IDT's contractual rights.[25] While having a high potential face value, the settled claim had a low chance of success. The Court valued it at approximately $1.5 million less than what IDT had paid in settlement. Still, applying the unified entire fairness standard, the fair price was insufficient to overcome the controller's flagrant breach of duty. But, given the settlement's fair price, the plaintiffs recovered only nominal damages.

Key Takeaways: *Straight Path* reinforces that fiduciaries involved in a conflicted controller transaction with process flaws may nonetheless substantially prevail at trial if they can demonstrate fairness in the price.

25 *Id.* at *19.

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