Byron F. Egan, How Recent Fiduciary Duty Cases Affect Advice to Directors and Officers of Delaware and Texas Corporations, 37th Annual Conference on Securities Regulation and Business Law (Dallas, Tex., Feb. 13, 2015), citing Bigler & Tillman's Void or Voidable -- Curing Defects in Stock Issuances Under Delaware Law

Seth Barrett Tillman
HOW RECENT FIDUCIARY DUTY CASES AFFECT
ADVICE TO DIRECTORS AND OFFICERS OF
DELWARE AND TEXAS CORPORATIONS

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Under Delaware law, the question remains, however, whether approval by a majority of disinterested stockholders will, pursuant to DGCL § 141(2), cure any invalidity of director actions and, by virtue of the stockholder ratification, eliminate any director liability for losses from such actions. In Ganter v. Stephens, the Delaware Supreme Court found that stockholder approval of a going private stock reclassification proposal did not effectively ratify or cleanse the transaction for two reasons:

First, because a shareholder vote was required to amend the certificate of incorporation, that approving vote could not also operate to "ratify" the challenged conduct of the interested directors. Second, the adjudicated cognizable claim that the Reclassification Proxy contained a material misrepresentation, eliminates an essential predicate for applying the doctrine, namely, that the shareholder vote was fully informed.

In Ganter, the Court in effect held that stockholder ratification of a transaction that was voidable because of director fiduciary duty breaches in its approval did not validate the transaction. If, however, the stockholders had in an express and separate ratification vote (after full disclosure) ratified the action, the transaction would have been cleansed of breaches of fiduciary duty even if a vote is required by statute and revive the presumptions of the business judgment rule.

Since Ganter only dealt with the infection of action by a conflicted board of directors, Ganter does not address holdovers of earlier cases regarding the distinction between void and voidable actions, and leaves standing the concept that a void action cannot be ratified so as to give it the retroactive effect of validating the action from the original date. In earlier cases, the Delaware courts have held that a void act (e.g. a ultra vires action or an action that does not comply with law or governing documents) cannot be ratified, and thus given retroactive sanctification and effect.

XII. Asset Transactions.

A. Shareholder Approval.

A sale or exchange of all or substantially all of the assets of an entity may require approval of the owners depending on the nature of the transaction, the entity’s organization documents and applicable state law. In most states, shareholder approval of an asset sale has historically been required if the corporation is selling all or substantially all of its assets.

I. DGCL.

The Delaware courts have used both “qualitative” and “quantitative” tests in interpreting the phrase “substantially all,” as it is used in DGCL § 271, which requires stockholder approval for a corporation to sell, lease or exchange all or substantially all of its property and assets.

In Hollinger Inc. v. Hollinger International, Inc., the sale of assets by a subsidiary with approval of its parent corporation (its stockholder), but not the stockholders of the parent, was alleged by the largest stockholder of the parent to contravene DGCL § 271. Without reaching a conclusion, the Chancery Court commented in dicta that “[w]hen an asset sale by the wholly owned subsidiary is to be consummated by a contract in which the parent entirely guarantees the performance of the selling subsidiary that is disposing of all of its assets and in which the parent is liable for any breach of warranty by the subsidiary, the direct act of the parent’s board can, without any appreciable stretch, be viewed as selling assets of the parent itself.” The Chancery Court acknowledged that the precise language of DGCL § 271 only requires a vote on covered sales by a corporation of “its assets, but found that analyzing

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1318 See supra notes 272-280 and related text.

See PRINCIPLES OF CORPORATE GOVERNANCE: ANALYSIS AND RECOMMENDATIONS § 8.03 (American Law Institute 2000). "The Reorganization Proxy Statement, as amended, describes the nature of the proposed reorganization that would result from the execution of the Plan, the compensation of directors and their compensation as an officer of the Corporation and the rights of holders of the Corporation’s common stock (the "Proposal") that are necessary to ratify the action by the stockholders."

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