DELAWARE HODGEPodge: A REVIEW OF FREQUENT QUESTIONS
DELAWARE LAW PRACTITIONERS RECEIVE REGARDING PRIVATE EQUITY
AND VENTURE CAPITAL

Thursday, March 28, 2019, 2:30PM – 4:30 PM
East Meeting Level, Room 8

Over the years, the Private Equity and Venture Capital Committee has sponsored programs analyzing several of the “big issues” under Delaware law for Private Equity and Venture Capital, including the existence of conflicts, exit rights, and traps for the unwary in drafting preferred stock terms. This CLE will tackle several smaller, though no less important, issues. This “hodgepodge” of issues includes questions Delaware practitioners get asked on a regular basis, none of which standing alone would be the basis of a full CLE program, but in the aggregate will, we hope, provide participants with much to think about in their practices going forward. Among other topics, we will address the following:

Transfer Restrictions: Section 202 of the Delaware General Corporation Law (the “DGCL”) allows Delaware corporations to impose transfer and ownership restrictions on corporate securities. Under Section 202(b) of the DGCL, such restrictions may be imposed “by the certificate of incorporation or by the bylaws or by an agreement among any number of security holders or among such holders and the corporation.” However, “no restrictions so imposed shall be binding with respect to securities issued prior to the adoption of the restriction unless the holders of the securities are parties to an agreement or voted in favor of the restriction.” In many venture- and private equity-backed companies, the stockholders are parties to agreements containing transfer restrictions. In many cases, those restrictions may be amended by the holders of a majority of the stock subject to the transfer restrictions. Can stockholders not acceding to an amendment that broadens an existing transfer restriction be bound by that amendment? Does the answer depend on the breadth of the amendment? We will explore those questions on the panel.

Section 220 Information Rights: Section 220 of the DGCL grants stockholders the right to examine a corporation’s books and records for any “proper purpose”, which may include simply determining the value of a person’s equity. Caspian Select Credit Master Fund, Ltd. v. Key Plastics Corp., 2014 WL 686308 (Del. Ch. Feb. 24, 2014). Many venture- and private equity-backed companies, however, have an interest in keeping their books and records confidential. The panel will explore the potential for a stockholder to waive in advance in Section 220 information rights, including through a discussion of Schoon v. Troy Corp., 2006 WL 1851481 (Del. Ch. June 27, 2006) and Kortrum v. Webasto Sunroofs Inc., 769 A.2d 113 (Del. Ch. 2000).

Pay-to-Play: “Pay-to-Play” provisions, often utilized in dilutive financings, generally reward existing investors participating in a new round of financing and punish investors that do not so participate. The form of the punitive features of pay-to-play provisions vary, but two issues are common to many forms: (i) whether any series or class votes are necessary to institute the pay-to-play provisions and (ii) whether the pay-to-play provisions violate the “doctrine of equal treatment”.


With respect to the first issue, Section 242(b) of the DGCL grants holders of a class of stock the right to vote on an amendment that would “alter or change the powers, preferences, or special rights of the shares of such class so as to affect them adversely” and further provides that if an amendment would “alter or change the powers, preferences or special rights of 1 or more series of any class to as to affect them adversely, but shall not so affect the entire class,” then only the shares of the affected series are considered a class for this purpose. In addition, many charter provisions grant express class- or series-votes on charter amendments that adversely affect the class or series. We will explore the limited Delaware case law on what constitutes an “adverse effect” and whether the institution of various forms of pay-to-plays triggers such separate votes.

With respect to the second issue, the doctrine of equal treatment is a general notion that, under Delaware law, shares of stock of the same type, class or series should be treated equally. See, e.g., In re Sea-Land Corp. S’holders Litig., 642 A.2d 792, 799 (Del. Ch. 1993). The doctrine has more bite in certain areas than others. Compare Telvest, Inc. v. Olson, 1979 WL 1759 (Del. Ch. Mar. 8, 1979) (rounding up in connection with dividend of stock impermissible) with Nixon v. Blackwell, 1991 WL 194725 (Del. Ch. Sept. 26, 1991). How much bite does the doctrine have in the context of a pay-to-play is another issue the panel will explore.

Section 144: Section 144 of the DGCL is a statute designed to prevent certain interested transactions from being deemed per se invalid under Delaware law. The panel will explore the intended purpose of Section 144, how the Courts and practitioners have utilized Section 144, and whether that utilization is, in fact, in accordance with Section 144’s intended purpose.

Corporate Opportunity Waivers and Information Sharing: The “corporate opportunity” doctrine provides that a corporate officer or director may not take a business opportunity for his or her own if (1) the corporation is financially able to exploit the opportunity, (2) the opportunity is within the corporation’s line of business, (3) the corporation has an interest or expectancy in the opportunity, and (4) by taking the opportunity for his or her own, the corporate fiduciary will thereby be placed in a position inimical to his or her duties to the corporation. Broz v. Cellular Info. Sys., Inc., 673 A.2d 148, 154-55 (Del. 1996). Delaware law allows a corporation to renounce any interest or expectancy of the corporation in, or in being offered an opportunity to participate in, specified business opportunities or specified classes or categories of business opportunities that are presented to the corporation or one or more of its directors or officers, thus effectively “waiving” the corporate opportunity doctrine as to such renounced interests. 8 Del. C. § 121(17). Notwithstanding such a waiver, directors continue to owe a fiduciary duty of confidentiality to a corporation. The panel will explore the scope of corporate opportunity waivers, how they interact with the duty of confidentiality, and exceptions to the duty of confidentiality, including the right of blockholder designees to share information with the funds that designated them.

Corporate Action Via Electronic Means: Corporate law has made efforts to keep up with the transformation to the digital age. The panel will explore the methods available to corporations to act via electronic means.