



## Recent Amendments to Delaware General Corporate Law Allow for Bylaw Provisions Granting Shareholder Access to Proxy Materials

Shareholder access to public company proxy ballots has been a highly controversial issue in the ongoing debate concerning the appropriate balance of power between corporate boards and their shareholders. On April 10, 2009, Delaware signed into law certain amendments to the Delaware General Corporate Law (DGCL) relating to the proxy process, which will take effect on August 1, 2009. These two new sections of the DGCL allow Delaware corporations to add provisions to their bylaws that would facilitate shareholder access to the corporations' proxy statements, but do not require the adoption of any new bylaw provisions.

### Background

In 2008, the Delaware Supreme Court held in the case of *CA, Inc. v. AFSCME Employees Pension Plan* that shareholder-adopted bylaws relating to procedures and processes for director elections were generally valid under the DGCL. Separately, the Securities and Exchange Commission has discussed (but did not adopt) proposed rules that would provide shareholders access to corporations' proxy statements for the purpose of nominating director candidates. For a time, it appeared that the issue of shareholder proxy access had stalled. Following the financial crisis, however, it seemed that federal lawmakers and regulators had again begun to focus on shareholders' access rights. The recent adoption of the amendments to the DGCL appears to reflect Delaware's desire to forestall legislation.

### Access to Proxy Materials

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### Contacts:

[Frank M. Placenti](#)  
+1.602.528.4004

[Joseph P. Richardson](#)  
+1.602.528.4801

[Ryan J. Kretschmer](#)  
+1.602.528.4823

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New §112 of the DGCL provides that a Delaware corporation may include a provision in its bylaws granting its shareholders access to the corporation's proxy materials in certain circumstances. Specifically, new §112 states that the corporation's bylaws may provide that, if the corporation solicits proxies with respect to the election of directors, shareholders' nominees must be included in such proxy solicitation materials. New §112 sets forth a nonexclusive list of procedures that a corporation can put in place to limit shareholder access to its proxy materials, including:

- A minimum level of stock ownership and/or a minimum duration of stock ownership;
- Requirements for the nominating shareholder to provide certain specified information about the shareholder and the nominee or nominees;
- Conditions for eligibility relating to the number or proportion of directors nominated or to whether the nominating shareholder previously sought access to the corporation's proxy materials;
- Exclusion of nominations in the event the nominating shareholder or the nominee has acquired or is related to the acquisition of a specified percentage of the corporation's shares within a specified period prior to the election of directors; and
- Requirements that the nominating shareholder indemnify the corporation for losses arising from any false or misleading information or statements submitted by such nominating shareholder.

### **Reimbursement of Shareholder Solicitation Expenses**

New §113 of the DGCL relates to reimbursement of shareholder solicitation expenses and provides that a Delaware corporation may include a provision in its bylaws allowing for the reimbursement of reasonable proxy solicitation expenses incurred by a shareholder soliciting proxies in connection with the election of directors. Similar to §112, the new §113 sets forth a nonexclusive list of conditions that the bylaws may impose upon the shareholders' right to reimbursement, including:

- Conditions for eligibility relating to the number or proportion of persons nominated by the shareholder seeking reimbursement or to whether the shareholder previously sought

reimbursement;

- Limitations on the amount of reimbursement based on the proportion of votes cast in favor of the requesting shareholder's nominees, or based on the amount spent by the corporation soliciting proxies in connection with the election of directors; and
- Limitations relating to the election of directors by cumulative voting.

## Implementation Considerations

While the amended provisions of the DGCL contain lists of limitations and exclusions intended to guide corporations when drafting the newly permitted bylaws, these lists are explicitly nonexclusive and certainly do not address all the potential pitfalls that may be encountered when drafting such provisions. For example, in the *CA, Inc. v. AFSCME* case discussed above, the court stated that the proposed bylaw in question, which related to reimbursement of shareholder solicitation expenses, could cause the directors to breach their fiduciary duties by requiring them, under all circumstances, to reimburse such expenses. The court further stated Delaware law requires that such a bylaw contain a "fiduciary out" allowing the directors to determine on a case-by-case basis whether reimbursement would be appropriate. The nonexclusive list of conditions in the newly adopted §113 does not include any such explicit "fiduciary out." Directors may also wish to consider other restrictions relating to the good faith of the proponents.

In addition, the fact that the amendments to the DGCL do not explicitly list permitted exclusions and limitations gives corporations considerable leeway in drafting new bylaw provisions. Given such leeway, corporations should thoughtfully consider whether to adopt provisions enabling shareholder proxy access. If such access is provided, bylaws should be carefully prepared to define the processes for director nomination and shareholder proposals. In addition, corporations should take steps to gain a solid understanding of their shareholder base and should be aware of any shifts that may have occurred as a result of the recent economic environment.

## Conclusion

In deciding whether to adopt access bylaw provisions, corporations should evaluate the benefits of such provisions and weigh them against the potential costs and drawbacks. In the absence of such provisions, corporations may be approached by shareholders

demanding that such bylaw provisions be adopted, and such shareholders may seek to include shareholder proposals relating to the adoption of such bylaw provisions in materials for upcoming annual meetings. In such cases, it may be more difficult to craft suitably balanced bylaw provisions.

For further information relating to the amendments to the DGCL, or advice on drafting the newly allowed bylaw provisions or responding to shareholder requests and proposals, please contact your principal Squire Sanders lawyer or any of the individuals listed in this Alert.

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Two Renaissance Square, 40 North Central Avenue, Suite 2700, Phoenix, Arizona 85004

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