BLASIUS, BYLAW AMENDMENT POWERS & SUPERMAJORITY AMENDMENT BYLAWS

J.S. PARK[*]

ABSTRACT

This paper considers whether under Delaware law a shareholder can defeat a supermajority amendment bylaw unilaterally adopted by a corporation's board of directors. It argues that the principles developed in *Blasius Industries, Inc. v. Atlas Corp*. are persistent and may reemerge to empower plaintiff shareholders and shareholder activists to strike down such a bylaw. It is further inferred that "*Blasius* principles" could be used against a supermajority amendment bylaw unilaterally adopted by a board. This position takes into account the unsettled allocation of bylaw amendment powers under Delaware law as well as the challenge posed to Delaware's board-centrism.

TABLE OF CONTENTS

[*] J.S. Park, B.C.L., LL.B., is a graduate of the McGill Faculty of Law and pursuing articles of clerkship at Dentons LLP in Montreal.

I. INTRODUCTION

Under Delaware law, may a shareholder defeat a supermajority amendment bylaw ("SAB")—a provision requiring an enhanced plurality of equity voting interests to amend the bylaws—that was unilaterally adopted by a corporation's board of directors?

While the question appears to have been resolved in the affirmative almost two decades ago in *Chesapeake Corp. v. Shore*[1], substantial uncertainty remains in part because the *Blasius* heightened standard of review applied then has since been reformulated to disadvantage shareholders. Despite this uncertainty and disadvantage, the standard developed in *Blasius Industries, Inc. v. Atlas Corp.*[2]

---

1 *See* Chesapeake Corp. v. Shore, 771 A.2d 293 (Del. Ch. 2000).
2 *See* Blasius Industries, Inc. v. Atlas Corp., 564 A. 2d 651 (Del. Ch. 1988).

may reemerge to empower plaintiff shareholders to strike down a SAB unilaterally adopted by a board of directors. This paper argues that *Mercier v. Inter-Tel*[3] did not repudiate the principles of shareholder enfranchisement vested in the original *Blasius* decision when it reformulated the *Blasius* test; its chief achievement was to dilute the standard's functional application without entirely restricting the principles embedded in it. The "*Blasius* principles" may thus be used against a SAB unilaterally adopted by a board, particularly given how unsettled the allocation of the power to amend bylaws is under Delaware law and given how these principles challenge Delaware's board-centrism.

This paper briefly introduces SABs then describes Delaware's general treatment of SABs in Part II and III respectively. Part IV examines post-*Chesapeake* developments, analyzing the *Blasius* reformulation and its consequences. Specifically, it discusses the dilution of the review standard, the muddled attempt to confine its use to specific categories, and the preservation of the "Blasius principles", as defined further below. Part V details the principles and Part VI highlights how the reformulation could present difficulties if a situation like *Chesapeake* appeared today. Lastly, Part VII argues the *Blasius* principles could fill a vacuum that exists in Delaware law with respect to the power to amend bylaws, and further, that the principles are designed to legitimately challenge the board-centrism towards which the *Blasius* reformulation is fashioned to gravitate.

II. SUPERMAJORITY AMENDMENT BYLAWS ("SABS")

Supermajority requirements imposed on shareholders to amend bylaws work to undermine shareholders. By increasing the threshold necessary to overcome decisions (usually to a two-thirds requirement but not necessarily so), SABs do three things. First, they help maintain the *status quo*. Second, they may erect an onerous barrier that shields other bylaws that contravene shareholder interests (e.g. staggered boards, procedures relating to the nomination of directors, corporate policy, and a host of other rules that impact the balance of power between management and shareholders). Third, SABs may tend toward entrenching management.

Conversely, in addition to strengthening the corporation's negotiating position in an anti-takeover scenario and acting as a shark repellent, SABs may play a benevolent role. An amendment to the bylaws is an event of sufficient importance to require a non-ordinary number of shareholders to have a say in the matter. Those espousing this view would argue that an amendment to bylaws is akin, if not equivalent, to an amendment to the articles of incorporation. Proponents of SABs would claim they help preserve and maximize value for all shareholders by ensuring important decisions are taken only when they clearly represent the will of the shareholder franchise. This principle is also reflected in the political realm

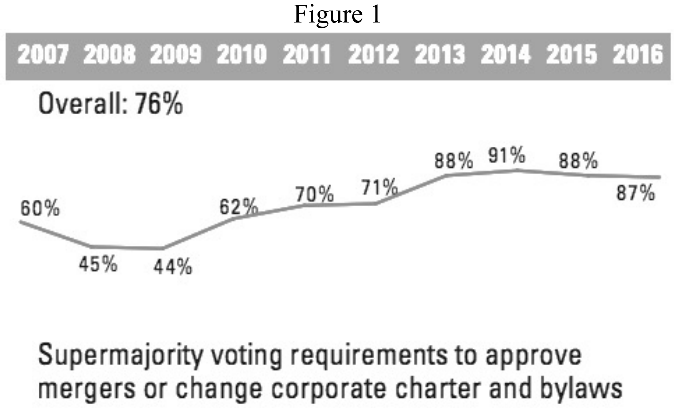
---

[3] *See* Mercier v. Inter-Tel (Del.), Inc., 929 A.2d 786 (Del. Ch. 2007).

where many legislative bodies require elevated approval thresholds. In corporate law, the British Columbia *Business Corporations Act* seems to accept this line of reasoning, as it omits distinguishing bylaws from articles of incorporation and effectively requires a special resolution of the shareholders to amend either.[4] Further, there may be overlap as to what is each covered by corporate bylaws and the articles.

In *What Matters in Corporate Law*, Bebchuk identified limits to the shareholders' power to amend bylaws as one of six discrete components highly correlated with poor corporate governance.[5] For this reason alone, this paper should be of theoretical interest. As I will discuss, the power to amend bylaws engages broader questions relating to corporate law and the appropriate scope of power bestowed to two key constituents—stockholders and directors. But equally important, as Bebchuck observed, bylaws have practical effects. Although limits on the shareholders' power to amend bylaws in the form of supermajority voting requirements are viewed negatively by institutional proxy firms, most companies that undergo an initial public offering (IPO) have supermajority amendment provisions and their inclusion among IPO companies has been on an upward trend since 2007.[6] According to a survey by WilmerHale, 87% of IPO companies in 2016 included supermajority voting requirements to approve mergers or corporate charter and bylaws (see Figure 1).[7] On the S&P500, 150 companies have a SAB.[8] But perhaps more to the point, should boards feel unconstrained, many companies would no doubt seek to have them ratified.

Figure 1



4 Business Corporations Act, S.B.C. Reg. 65/259(2) (Can).
5 *See* Lucian A. Bebchuk, Alma Cohen & Allen Ferrell, *What Matters in Corporate Governance?*, 22 REV. FIN. STUD. 783, 783-827 (2009).
6 WILMER CUTLER PICKERING HALE AND DORR LLP, 2017 M&A REPORT (2017), https://www.wilmerhale.com/uploadedFiles/Shared_Content/Editorial/Publications/Documents/2017-WilmerHale-MA-Report.pdf.
7 *Id.*
8 *See* Standard & Poor's Capital IQ database.

III. SABs UNDER DELAWARE LAW

A. Background

The initial bylaws of a corporation are adopted at the incorporation stage by the incorporator or the initial directors. The Delaware General Corporation Law ("*DGCL*") provides that only shareholders subsequently have the power to amend bylaws unless the articles of incorporation expressly confer that power on the board of directors. Bylaws authorizing the board of directors to amend bylaws do not divest the shareholders of their residual power to amend bylaws. By contrast, the articles of incorporation may be amended through a three-step process: the board of directors first recommends the amendment to the shareholders; it then becomes incumbent on a majority of the shareholders eligible to vote to approve or disapprove the amendment; lastly, if the amendment is approved, it must be filed with the Secretary of State.[9] In practice, many corporations will allow both the board of directors and the shareholders to amend bylaws.

B. Difficulty in breaking ratified SABs

Case law has consistently upheld supermajority voting requirements in various corporate situations.[10] The Supreme Court of Delaware, in upholding an 80% supermajority, held that in order to change the default majority rule in a vote on the election of directors, a supermajority provision must be "clear and unambiguous" or else becomes ineffective.[11]

Moreover, corporate bylaws are presumed valid and a court will attempt to construe the bylaws in a manner consistent with law. Thus, the plaintiffs' burden in a challenge to the statutory and contractual validity of the bylaws is a high one: they must show that the bylaws cannot operate lawfully or equitably under any circumstances.[12]

As the Supreme Court of Delaware made clear, the bylaws of a Delaware corporation constitute part of a binding contract between the directors, officers, and stockholders formed within the statutory framework of the *DGCL*. This contract is by design flexible and subject to change in the manner that the *DGCL* spells out, which investors know about when they purchase stock in a Delaware

---

[9] DEL. CODE ANN. tit. 8, §242(c) (2017).
[10] *See generally* R. Franklin Balotti & Jesse A. Finkelstein, DELAWARE LAW OF CORPORATIONS & BUSINESS ORGANIZATIONS, (3rd ed. 2016).
[11] Centaur Partners, IV v. National Intergroup, Inc., 582 A.2d 923 (Del. 1990).
[12] *See* Boilermakers Local 154 Ret. Fund v. Chevron Corp., 73 A.3d 934, 938 (Del. Ch. 2013).

corporation. Under this theory, ratified bylaws (including supermajority bylaws) that are consistent with the *DGCL* and equity will not be voided.[13]

Finally, Delaware corporate law has long rejected the so-called "vested rights" doctrine. That vested rights view asserts that boards cannot modify bylaws in a manner that arguably diminishes or divests pre-existing shareholder rights absent stockholder consent. Under Delaware law, where a corporation's articles or bylaws put all on notice that the by-laws may be amended at any time, no vested rights can arise that would contractually prohibit an amendment.[14]

C. Precedent to enjoin a prospective or recent board-adopted SAB

Precedent exists for shareholders to block a prospective SAB or strike a recent SAB unilaterally adopted by a board. In *Chesapeake v. Shore*, the board of directors of the defendant corporation, Shorewood, faced a takeover and implemented a slew of defensive measures. These included a staggered board, the removal of stockholder rights to call special meetings, and a bylaw stipulating that 66 2/3% of the outstanding shares had to approve an amendment. Notably, the company had a poison pill in place that was subject to the voting threshold. The board justified its actions by arguing that it was seeking more favorable terms for the proposed transaction in response to the threat of price inadequacy. It also sought to address the threat of stockholder confusion in relation to the transaction. The Court of Chancery struck down the SAB on two grounds: (i) the board's action failed to withstand *Unocal* enhanced scrutiny because the SAB was a defensive measure adopted disproportionately in relation to a threat found unreasonable; and (ii) the board's action contravened enhanced scrutiny under *Blasius* because the board acted with the primary purpose of interfering with or impeding the stockholder franchise without a compelling justification.[15]

The decision is noteworthy for several reasons. First, *Chesapeake* is the leading case on SABs. Second, it shows the court applying the *Unocal* and *Blasius* standards of review conjointly and, in the process, wrestling with its previous decision in *Stroud v. Grace*[16] (which effectively subsumed *Blasius* into Unocal). It expressly considered just how far-reaching *Blasius* ought to be when working with *Unocal*, raising the need for additional clarity on the milestone doctrinal unification of *Blasius* and *Unocal*.[17] Notwithstanding this longing for clarity, then-Vice Chancellor Strine, ultimately presented a unified standard with the following hybrid scope:

---

13 *See id.*at 949.
14 *See id.*at 955.
15 *See* Chesapeake Corp. v. Shore, 771 A.2d 293, 296 (Del. Ch. 2000).
16 *See* Stroud v. Grace, No. 10719 1990 Del. Ch. LEXIS 185.
17 *Chesapeake Corp.*, 771 A.2d 293 at 317-18, 324.

> If *Unocal* is applied by the court with a gimlet eye out for inequitably motivated electoral manipulations or for subjectively well-intentioned board action that has preclusive or coercive effects, the need for an additional standard of review is substantially lessened. . .it may be optimal simply for Delaware courts to infuse our *Unocal* analyses with the spirit animating *Blasius* and not hesitate to use our remedial powers where an inequitable distortion of corporate democracy has occurred.[18]

Though the Vice Chancellor recognized that the "compelling justification" standard of *Blasius* had been eschewed in certain precedents, he nevertheless hedged bets and applied *Blasius* as part of the *Unocal*/*Unitrin* framework as well as separately. Still, the language of the decision may lead one to conclude that the shareholders in the case prevailed under both *Unocal* and *Blasius* independently even if both standards of review were also applied as one. As the Vice Chancellor held: "I conclude that the defendants have not met their burden to sustain the Supermajority Bylaw under either the *Unocal v. Mesa Petroleum Co.* or *Blasius Indus. v. Atlas Corp.* standards of review."[19] On this ground, the Court of Chancery later made repeated attempts to address this apparent dissonance that led to a reconfiguration of the *Blasius* test.

IV. *BLASIUS* POST-*CHESAPEAKE*

Post-*Chesapeake* decisions show a clear attempt to rein in the flaws in *Blasius*. The test itself was only applied rarely, and from the time of its creation, the Court of Chancery worked on devising a unified workable standard of review under *Unocal*. In doing so, the Delaware court revealed its aversion to *Blasius*, mainly for practical reasons, ultimately leading it to reformulate *Blasius* in *Mercier*. This section will survey the alteration and illustrate that the *Blasius* standard of review splintered into (A) a diluted test within *Unocal/Unitrin,* (B) an ambiguous attempt at limiting the application of *Blasius* to certain categories of cases, and finally, (C) a set of valid principles in force under *Unocal*/*Unitrin*. Together, these three aspects produced considerable uncertainty.

A. Blasius*: Reformulated & diluted*

In *Mercier v. Inter-Tel*, the Court of Chancery dealt with a board decision to postpone a meeting and set a new record date in the context of a merger.[20] It reformulated *Blasius* by subsuming it under *Unocal*—a move the court claims

---

[18] *Id.* at 323.
[19] *Id.* at 297.
[20] *See* Mercier v. Inter-Tel (Del.), Inc., 929 A.2d 786 (Del. Ch. 2007).

was consistent with the "directional teachings" of three prominent decisions featuring *Blasius*, including *Chesapeake*.[21] The reformulation thus involved applying "a reasonableness standard consistent with the *Unocal* standard which required that the board of directors in *Mercier* (1) identify a "legitimate corporate objective" that was "proper and not selfish" (the "reasonableness" branch of the test) and (2) show that the board's actions were reasonable "in relation to their legitimate objective" and "did not preclude the stockholders from exercising their right to vote or coerce them into voting a particular way (the "proportionality" branch).[22]

This reformulation achieved two things as a matter of form: First, the "legitimate corporate objective" approach effectively displaced "the primary purpose" standard originally promulgated by *Blasius*. Second, it disrupted in part the "compelling justification" standard from *Blasius* while being careful not to entirely dispense with it. Notwithstanding its dismantling of the *Blasius* test, the court still went on to apply the "compelling justification" standard because it was bound by the Supreme Court of Delaware's *MM Cos. v. Liquid Audio*[23] decision that upheld it.

In its reasons, the Court of Chancery forcefully justified its reformulation of *Blasius* by identifying the following problems: *Blasius* assumed a result instead of providing for an inquiry[24]; the "compelling justification" standard was too stringent[25]; prior decisions supported a parallel relationship between *Blasius* and *Unocal*; and finally, *Blasius* was not well suited to situations where the board would continue holding office.[26]

This reformulation represents a sharp dilution of the *Blasius* test. As part of *Unocal*, the standard of review is not only more board-centric (in the plain sense that it focuses on the actions of the board as opposed to starting its analysis from the point of view of the shareholder franchise) but also more board-friendly because it discourages the strict "compelling justification" standard in favor of more relaxed exculpatory standards ("reasonableness" and "proportionality"). Some have commented that it is the threat to the presumption of propriety under the business judgment rule which was problematic about *Blasius*. As Hutchison wrote:

> Cases confirm that the *Blasius* framework presents its own difficulties, including the possibility that the language that cabins

---

21 *Id.* at 788.
22 *Id.* at 810-11.
23 *See generally* MM Cos. v. Liquid Audio, Inc., 813 A.2d 1118 (Del. 2002).
24 *Mercier*, 929 A.2d at 807.
25 *Id.* at 806.
26 *Id.* at 808.

> the *Blasius* standard may serve as a basis to demolish a reasoned conception of the business judgment rule that envisions directorial authority as the correct solution to the problem of creating, managing, and monitoring a public corporation.[27]

Perhaps not coincidently, Chancellor Allen precisely sought to overcome the "formidable protections"[28] of the business judgment rule in *Blasius*, perceiving that the board's impugned decisions were carried out honestly and competently.[29] As this paper details in Part V, the inclusion of the *Unitrin* standard of "preclusiveness" is said to be a sufficient substitute post-*Blasius* for the purpose laid out by Chancellor Allen in *Blasius*; however, this view also presents its own set of problems.

B. Muddled scope of applicability

In *Mercier*, Vice Chancellor Strine expressed unease with *Blasius'* expansiveness and attempted to confine its applicability to matters relating to the election of directors and to matters touching on issues of control.[30] In the main, he stated that *Blasius* was "far less powerful" when it has "little to no bearing" on "whether the directors will continue in office". This was expressly supported by taking issue with the proposition that *Blasius* could apply to "all stockholder votes". The Vice Chancellor further argued that directors are not expected to be "neutral" with regards to matters proposed for shareholder action.[31] With respect to matters of control, he explained how *Blasius* ran roughshod outside the corporate control context. Specifically, the Vice Chancellor pointed out that post-*Blasius* cases wrestled with the reality that directors will inevitably be partial and show "discomfort about using such a stringent standard of review in circumstances when a stockholder vote has no bearing on issues of corporate control."[32] However, there are several problems with this classification effort.

First, the Vice Chancellor cited two cases in particular which present nuance: *In re MONY Group Inc. S'holder Litig.*[33] and *State of Wisconsin Inv. Bd. v. Peerless*

---

[27] Harry G. Hutchison, *Director Primacy and Corporate Governance: Shareholder Voting Rights Captured by the Accountability/Authority Paradigm*, 36 LOYOLA U CHI. L.J. 1111, 1126 (2005).

[28] Blasius Industries, Inc. v. Atlas Corp., 564 A.2d 651, 657 (Del. Ch. 1988).

[29] *Id.* at 660.

[30] "Frankly, I do not believe that this test should be used as to director conduct not affecting either an election of directors or a vote touching on matters of corporate control. This test is a potent one that should not be used in garden variety situations, when more traditional tools are available to police self-dealing or improperly motivated director action."
Mercier, 929 A.2d at 811.

[31] *Id.* at 809.

[32] *Id.*

[33] *See* In re MONY Group Inc. S'holder Litig., 853 A.2d 661 (Del. Ch. 2004).

Sys. Corp.[34] In the former the court acknowledged that *Blasius* "did not easily or readily apply" to issues touching on "directorial control, as its demanding standard could unduly limit the legitimate exercise of directorial power and discretion in other contexts."[35] This passage, however, is followed by the explicit recognition by Vice Chancellor Lamb that "<u>in any voting context</u>, actions taken for the purpose of interfering with a full and fair exercise of the stockholder franchise will run afoul of basic equitable limitations found in our law. *Schnell,* 285 A.2d 437" (emphasis added).[36] Similarly, the Vice Chancellor cited as support the recital of the facts in *Peerless* which involved an adjournment of an annual meeting of shareholders. The court in *Peerless* did not find a primary purpose of interference with the shareholder franchise; however, the Chancellor only granted that *Blasius* was "admittedly wrapped in lofty idealism" and "often difficult to apply to the practicalities of corporate governance."[37] The Chancellor deferred to the precedence set forth in *Blasius* as it was handed down by the courts:

> As the earlier discussion of shareholder vote sanctity attempted to demonstrate, *Blasius* does not only apply in cases involving hostile acquirers or directors wishing to retain their position against the will of the shareholders. The derivation of board power from shareholders, as well as the allocation of power with respect to governance of the corporation, are broad structural concerns within the corporate form that are present <u>in any shareholder vote</u>. The fiduciary duty of loyalty between a board of directors and the shareholders of a corporation is always implicated where the board seeks to thwart the action of the company's shareholders.[38]

Equally significant, Chancellor Chandler welcomed *Blasius* and the ensuing real world consequence of greater shareholder assertiveness against corporate management as embodying a "bedrock foundation for directorial power" and as constituting a "wholesome development," respectively.[39] Though Vice Chancellor Strine in *Mercier* attempted to hold that *Blasius* should apply to director elections and matters of control exclusively, *Peerless* can only weakly stand for the proposition.

---

34 *See* State of Wisconsin Inv. Bd. v. Peerless Sys. Corp., No. 17637, 2000 Del. Ch. LEXIS 170 (Del. Ch. Dec. 4, 2000).
35 *In re MONY Group Inc. S'holder Litig.*, 853 A.2d at 681 n.51.
36 *Id.*
37 *Peerless*, 2000 Del. Ch. Lexis 170, at 44.
38 *Id.* at 43-44.
39 *See id.* at 66-68.

Even taken together, *Peerless* and *In re MONY* are inconsistent with *Mercier*. First, *In re MONY* explicitly acknowledged that *Blasius* could be applied outside a directorship election "in circumstances in which self-interested or faithless fiduciaries act to deprive stockholders of a full and fair opportunity to participate in the matter and to thwart what appears to be the will of a majority of the stockholders," as in [*Peerless*].[40]

Second, the reasoning seems perpendicular to the Supreme Court of Delaware and its opinion in *Liquid Audio,* which held that *Gilbert*, a prior decision propelling the doctrinal unification of *Blasius* and *Unocal*, did not "render *Blasius* and its progeny meaningless."[41] *Liquid Audio* restated *Blasius* as a matter of principle beyond the subject-matter at bar:

> At issue in this case is not the validity generally of either a bylaw that permits a board of directors to expand the size of its membership or a board's power to appoint successor members to fill board vacancies. In this case, however, the incumbent Board timed its utilization of these otherwise valid powers to expand the size and composition of the Liquid Audio board for the primary purpose of impeding and interfering with the efforts of the stockholders' power to effectively exercise their voting rights in a contested election for directors. As this Court held more than three decades ago [in *Schnell*], 'these are inequitable purposes, contrary to established principles of corporate democracy . . . and may not be permitted to stand.'[42]

The attempt in *Mercier* to confine *Blasius* still had an effect, and there have been cases parallel to *Mercier* which led to a narrowed scope of application for *Blasius*. Jacob Kling argued that the effect of *Mercier*'s alteration of *Blasius* had been to restrict *Blasius* to entrenchment cases.[43]

As I address later in this paper, this confusing state of affairs could confound a re-application of *Blasius* as it was applied in *Chesapeake* to a future case involving a SAB because it is unclear that a SAB necessarily qualifies as a non-entrenchment measure and it is further unclear how future cases will fit, if at all, within the ordering project described above.

---

[40] In re MONY Group Inc. S'holder Litig., 853 A.2d 661, 674 (Del. Ch. 2004).

[41] MM Cos. v. Liquid Audio, Inc., 813 A.2d 1118, 1130 (Del. 2003).

[42] *Id.*at 1132.

[43] *See* Jacob A. Kling, Note, *Disenfranchising Shareholders: The Future of Blasius After Mercier v. Inter-Tel*, 119 YALE L.J. 2040 (2010).

C. The preservation of principles

Post-*Mercier* cases re-affirm the dilution of the *Blasius* test and its putative restriction to cases involving the election of directors or touching on matters of control.[44] Notwithstanding, the principles at the heart of the original *Blasius* test (the "Blasius principles") subsist. Chancellor Allen, Vice Chancellor Jacobs and Vice Chancellor Strine co-authored a paper in 2001 in which they wrote that "the problem with *Blasius* is practical, not a matter of principle."[45] In retrospect, this may have been a harbinger of the principles' persistence. In *Kallick v. Sandridge Energy Inc.*[46], the Court of Chancery dealt with a proxy fight where the plaintiff shareholders claimed the directors of the defendant corporation breached their fiduciary duties by failing to approve a slate of directors proposed by a hedge fund for the purposes of a proxy put. Though Vice Chancellor Strine rejected the plaintiffs submission under *Blasius*, he wrote that the importance of the standard of review "rests more in its emphatic and enduring critical role in underscoring the serious scrutiny that Delaware law gives to director action that threatens to undermine the integrity of the electoral process, than in its articulation of a useful standard of review to decide actual cases."[47] While this surely represents yet another effort to constrain *Blasius* to matters involving the election of directors, the pronouncement begs the question: if we leave aside for a moment questions about its legitimate field of application, what does the "emphatic and enduring critical role" consist of exactly? As it happens, court efforts to contain *Blasius*, epitomized by *Mercier*, may have been insufficient—as the next part of this paper will illustrate by exploring what is emphatic and enduringly critical about *Blasius*.

V. WHAT IS THE "EMPHATIC AND ENDURING CRITICAL ROLE"?

This section discusses the *Blasius* principles and examines their integration with the *Unocal*/*Unitrin* standard of review. Specifically, it details five tenets that together form the principles and suggests how these tenets may legitimately reemerge to play an "emphatic and enduring critical" role.

A. Principle notwithstanding form

The *Blasius* principles may be traced back to the decision that conceived them—*Blasius Industries, Inc. v. Atlas Corp.* The case involved shareholders bringing actions challenging the board of directors' decision to add two members to the board of directors and to name a new majority of the board. Chancellor Allen

---

[44] *See, e.g.,* Johnston v. Pederson, 28 A.3d 1079 (Del. Ch. 2011).

[45] William T. Allen et al., *Function Over Form: A Reassessment of Standards of Review in Delaware Corporation Law*, 26 DEL. J. CORP. L. 859, 885 (2001).

[46] *See* Kallick v. Sandridge Energy, Inc. 68 A.3d 242 (Del. Ch. 2013).

[47] *Id.* At 258.

held that: (i) the evidence demonstrated that the incumbent directors were not acting out of a self-interested motive when they responded to a shareholder's proposal to increase the size of the board; (ii) the deferential business judgment rule did not shield directors' actions from scrutiny; (iii) the directors' actions in adding two members to the board was an unintended violation of shareholders' voting right; and (iv) election judges acted reasonably in limiting their count to written "ballots" before them and any errors in the count did not change the outcome of the consent solicitation process, under which the shareholders' proposal failed to garner a majority of the votes.[48]

Setting aside *Blasius'* perceived flaws, the case is notable for three reasons that form the essence of the *Blasius* principles. First, the *Blasius* test appeared here in a situation where corporate action was seen as interfering with the shareholder franchise without being self-interested. Whether the corporate threat in *Blasius* should have led the court to focus on the defensive nature of the board's actions and not its self-interested nature is another matter; it shows the court saw fit to focus on the subjective mindset of the board in relation to the shareholder vote as a general matter. Second, the court recognized that the board had reason to explain its actions, and the court further acknowledged that it acted in good faith.[49] But lastly, and above all, the court unequivocally affirmed an ideological defense of the shareholder franchise. For now, it suffices to reproduce the following words of Chancellor Allen's opinion, which captures the essence of the *Blasius* doctrine:

> The shareholder franchise is the ideological underpinning upon which the legitimacy of directorial power rests. . . [A] decision by the board to act for the primary purpose of preventing the effectiveness of a shareholder vote inevitably involves the question who, as between the principal and the agent, has authority with respect to a matter of internal corporate governance. . . Action designed principally to interfere with the effectiveness of a vote inevitably involves a conflict between the board and a shareholder majority. Judicial review of such action involves a determination of the legal and equitable obligations of an agent towards his principal. This is not, in my opinion, a question that a court may leave to the agent finally to decide so

48 *See* Blasius Industries, Inc. v. Atlas Corp., 564 A.2d 651 (Del. Ch. 1988).

49 "On balance, I cannot conclude that the board was acting out of a self-interested motive in any important respect on December 31. I conclude rather that the board saw the "threat" of the Blasius recapitalization proposal as posing vital policy differences between itself and Blasius. It acted, I conclude, in a good faith effort to protect its incumbency, not selfishly, but in order to thwart implementation of the recapitalization that it feared, reasonably, would cause great injury to the Company."*See id.* at 658.

> long as he does so honestly and competently; that is, it may not be left to the agent's business judgment.[50]

It may be inferred that the court presented this latter element because its other findings—e.g. the existence of good faith and a legitimate corporate objective—would save the impugned corporate actions under either the business judgment rule or *Unocal*'s reasonableness and proportionality standards.

Be that as it may, the Court of Chancery addressed flaws in *Blasius*, but it also simultaneously, in another sense, left the principles vested in the case undisturbed. In *Chesapeake*, Vice Chancellor Strine wrote that "it may be optimal simply for Delaware courts to infuse our *Unocal* analyses with the spirit animating *Blasius* and not hesitate to use our remedial powers where an inequitable distortion of corporate democracy has occurred".[51] Recognizing that "flavoring" differences between *Unocal* and *Blasius* did not justify the added doctrinal complexity created by continuing *Blasius* as a separate review standard, the authors of *Function Over Form* wrote that the post-*Blasius* experience showed that the *Unocal/Unitrin* analytical framework is "fully adequate to capture the voting franchise concerns that animated *Blasius*". Borrowing from *Chesapeake*, the authors added that this was so "*so long as the court applied Unocal with the gimlet eye* for inequitably motivated electoral manipulations or for subjectively well-intentioned board action that has preclusive or coercive effects"[52] (emphasis added). Those two views were produced almost contemporaneously around 2000-2001.

Despite the court's numerous confirmations that *Unocal* (together with *Unitrin* which incorporated preclusive effects to the shareholder franchise as functional substitutes to "interference" of the shareholder franchise in *Blasius*), the Court of Chancery has not repudiated the *Blasius* principles. As Vice Chancellor Strine wrote of the *Blasius* reformulation in *Mercier*, though the case represents an attempt to break from the *Blasius* line of decisions:

> I conclude that, consistent with the directional teaching of cases like *MM Companies, Inc. v. Liquid Audio, Inc.*, *In re MONY Group, Inc. S'holders Litig.*, and *Chesapeake Corp. v. Shore*, the Blasius standard should be reformulated in a manner consistent with using it as a genuine standard of review that is useful for the determination of cases[.][53]

---

[50] *Id.* at 659-60.
[51] Chesapeake Corp. v. Shore, 771 A.2d 293, 323 (Del. Ch. 2000).
[52] *See* Allen et al., *supra* note 45, at 890.
[53] Mercier v. Inter-Tel (Del.), Inc., 929 A.2d 786, 788 (Del. Ch. 2007).

B. The Blasius *principles*

Despite efforts to alter *Blasius* and despite the absence of guidance for an "emphatic and enduring critical role" for the *Blasius* principles as a practical and general matter outside the control and director election contexts*,* the conceptual basis of the principles enunciated by Chancellor Allen remains, albeit under a different form. As discussed above, despite the *Mercier* reformulation and in part because of the resulting instability, the following five precepts still stand (in addition to its central proposition that board action taken with the primary purpose of interfering with the shareholder franchise should be invalidated absent a compelling justification).

1. Legitimacy of directorial power rests with the shareholders

As Chancellor Allen wrote in *Blasius*, "the shareholder franchise is the ideological underpinning upon which the legitimacy of directorial power rests."[54] This point has been followed by subsequent cases and not explicitly foreclosed as a fundamental precept. The principles have also been taken to apply generally despite scope-narrowing efforts. Pro-*Blasius* cases like *Liquid Audio* and *In Re MONY* can be read, though only tenuously, to constrain the precept to the context of director elections or matters of control. But more recently, *Sandridge* relied on the principles as originally devised by *Blasius* and *Liquid Audio*. In doing so, it explicitly left open the door for the principles to apply to directorial power more generally:

> The most fundamental principles of corporate governance are a function of the allocation of power within a corporation between its stockholders and its board of directors. [5] The stockholders' power is the right to vote on specific matters, <u>in particular</u>, in an election of directors. The power of managing the corporate enterprise is vested in the shareholders' duly elected board representatives. [6] Accordingly, while these "fundamental tenets of Delaware corporate law provide for a separation of control and ownership," [7] the stockholder franchise has been characterized as the "ideological underpinning" upon which the legitimacy of the <u>directors managerial power</u> rests.[55] (emphasis added)

[54] Blasius Industries, Inc. v. Atlas Corp., 564 A.2d 651, 659 (Del. Ch. 1988).
[55] MM Cos. v. Liquid Audio, Inc., 813 A.2d 1118, 1126 (Del. 2003).

2. The *Blasius* principles are rooted in policy concerns regarding the allocation of power between directors and shareholders

In *Blasius,* Chancellor Allen pointed out that from a less generalized and doctrinal angle, the ordinary considerations to which the business judgment rule originally responded were not present in the shareholder voting context of the day, which faced the emergence of "the new institutional voices and arrangements that will make the stockholder vote a less predictable affair."[56] He also noted the inadequacy of limited choices facing shareholders (sell shares or vote to replace incumbents) and how novel institutional arrangements threatened the adequacy of this set of options.[57] Ultimately, for the Chancellor, this directly raised questions about the appropriate distribution of power between the board and shareholders.

Decisions continued to accept *Blasius* to support a general policy against shareholder disfranchisement in Delaware. *Peerless* recognized it because the shareholder franchise is the ideological underpinning upon which the legitimacy of directorial power rests and the right to vote one's shares is a fundamental aspect of stock ownership governed.[58] *Mercier* circumscribed the policy rationale to the election of directors, but as highlighted earlier in this paper, it could be argued that the policy motives delineated in dicta in *Liquid Audio* were not likewise limited.[59] Most recently, a decision by Court of Chancery reaffirmed the general policy role played by *Blasius* completely outside the narrow setting of director elections: in *Friends of the Vill. of Cinderberry,* Chancellor Allen found in favor of the unit holders of a non-profit association in their action against a developer which controlled associations belonging to the unit holders, "in the spirit of a different line of Delaware law."[60]

3. Judicial scrutiny may begin with an analysis of the effects on the shareholder franchise

As Kling wrote, the formulation of the *Blasius* standard compelling justification focuses on the board's purpose, but in practice Delaware courts will not engage in *Blasius* review if the board's action does not have a sufficient disenfranchising

---

56 *Blasius Industries, Inc.*, 564 A.2d at 659.
57 *See id.*
58 *See* State of Wisconsin Inv. Bd. v. Peerless Sys. Corp., No. 17637, 2000 Del. Ch. LEXIS 170, at*23-*24 (Del. Ch. Dec. 4, 2000). *See also In re MONY* Group Inc. S'houlder Litig., 853 A.2d 661.
59 *See* Mercier v. Inter-Tel (Del.), Inc., 929 A.2d 786, 808 n.63 (Del. Ch. 2007). See also *Liquid Audio*, 813 A.2d 1118, 1127 (Del. 2003) (stating that "The Courts of this State will not allow the wrongful subversion of corporate democracy by manipulation of the corporate machinery or by machinations under the cloak of Delaware law.").
60 *See* Friends of the Vill. of Cinderberry v. Vill. of Cinderberry Prop. Owners Ass'n, 2010 Del. Ch. LEXIS 83, at *29 (Del. Ch. May 5, 2010).

effect. The court will readily look at the effects of an allegedly disenfranchising act on the shareholder franchise and then on the subjective element of the inquiry under either the "primary purpose of interference" or the "legitimate corporate purpose" in good faith.[61] In *Chesapeake*, in conducting its inquiries under both *Blasius* and *Unocal*, Vice Chancellor Strine noted that the supermajority voting requirement demanded a margin never achieved by President Franklin Roosevelt before finding a primary purpose of interference.[62] Though the Court of Chancery dealt with this issue in *Mercier* (on the basis that *Blasius* presumed a result instead of providing for a method of inquiry), it may be argued that the "preclusiveness" inquiry—largely viewed to substitute *Blasius*'s purpose of protecting shareholder rights—similarly functions on the basis of finding factual preclusion of the shareholders' exercise of their voting rights.

4. Decisions by the board that are authorized by DGCL §141 but otherwise inequitable may not interfere with the shareholder franchise and may not encroach on its dominion over internal governance

Blasius suggests spheres of authority that could be within the purview of either directors or shareholders. It also suggests that the former could intrude on the rightful sphere of the latter—even when such authority was exercised honestly and competently. Specifically, *Blasius* suggests that shareholders had proper authority over the "internal governance" of the corporation. As Chancellor Allen wrote:

> A decision by the board to act for the primary purpose of preventing the effectiveness of a shareholder vote inevitably involves the question who, as between the principal and the agent, has authority with respect to a matter of internal corporate governance. . .Action designed principally to interfere with the effectiveness of a vote inevitably involves a conflict between the board and a shareholder majority. Judicial review of such action involves a determination of the legal and equitable obligations of an agent towards his principal. This is not, in my opinion, a question that a court may leave to the agent finally to decide so long as he does so honestly and competently; that is, it may not be left to the agent's business judgment.[63]

Board action carried out honestly and competently corresponds, in theory, to the good faith and legitimate corporate objective standard contained in the modified

---

61 *See* Kling *supra* note 43.
62 *See* Chesapeake Corp. v. Shore, 771 A.2d 293, 325-26 (Del. Ch. 2000).
63 Blasius Industries, Inc. v. Atlas Corp., 564 A.2d 651, 659-60(Del. Ch. 1988).

Blasius standard of review. Chancellor Allen articulates an expansive view of the shareholder franchise. This view may supersede proper board action in the event of interference with the franchise, whereupon the conflict between agent and principal would be laid bare and thereby require a regulation of the relationship, potentially in favor of the franchise.

5. Regard for the shareholder franchise has wide application

Blasius stands for the principle that that the shareholder franchise, as a matter of concern, should have broad application.There is no need to belabor the point here, which is covered above and in an earlier discussion criticizing the ordering effort in *Mercier*. It may be noted, however, that the Court of Chancery decision in *Johnston v Pedersen* recently reaffirmed *Mercier*.[64] The case involved the board's approval of a bridge loan convertible into Preferred Stock in an effort to dilute the voting rights of shareholders who sought to remove directors. In an otherwise typical *Blasius* case involving a contested election of directors, Vice Chancellor Laster interestingly relied on *Reis v. Hazelett Strip-Casting Corp*.[65], a statutory appraisal case reviving Blasius, as interpreted in *Peerless*. *Reis* stands for the proposition that *Blasius* enhanced scrutiny applies in situations other than election contests "where the law provides stockholders with a right to vote and the directors take action that intrudes on the space allotted for stockholder decision-making."[66] This may be taken as further evidence that the Court's effort to ring-fence the *Blasius* principles to matters relating to director elections and matters of control falls short. At the very least, it is additional proof that the principles have general applicability.

VI. PROBLEMS POSED BY THE REFORMULATION IN RELATION TO SABS

This part of the paper examines the implications of the reformulated Blasius test as it concerns SABs. Post-*Blasius* decisions have tried to refashion *Blasius* by incorporating its role into *Unocal*; but, a deeper analysis raises questions about whether this hybrid test would allow a court to enjoin a SAB in a case similar to *Chesapeake* today. This section will show that: (A) the "preclusiveness" standard in *Unocal/Unitrin* is not necessarily equivalent to the "primary purpose of interference" standard in *Blasius*; (B) a SAB could withstand scrutiny of the reformulated *Blasius* test because *Chesapeake* involved a peculiar set of factual circumstances that are not universal; finally, (C) even if we were to apply *Blasius* on a standalone basis, as it arguably was in *Chesapeake*, the systematic restricting of *Blasius* to cases of entrenchment could allow a board of directors to

---

64 *See* Johnston v. Pedersen, 28 A.3d 1079, 1089-91 (Del. Ch. 2011).
65 *See* Reis v. Hazelett Strip-Casting Corp., 28 A.3d 442 (Del. Ch. 2011).
66 *Id.* at 457.

successfully argue that SABs—or more precisely, increased voting thresholds to amend bylaws—do not invite a *Blasius* inquiry.

A. Unocal/Unitrin "preclusiveness" vs. Blasius *"primary purpose of interference"*

The "preclusiveness" standard in *Unocal/Unitrin* is not necessarily equivalent to the "primary purpose of interference" standard in *Blasius*. As part of the doctrinal merging effort, *Unocal*, insofar as it contains *Unitrin's* "preclusiveness" standard, succeeded at establishing a test equivalent to *Blasius*. As the judges wrote in *Function over Form*:

> *Unocal*—as refined by *Unitrin*—requires the court to decide whether any "defensive measure" (such as any attempt to manipulate a vote) is preclusive or coerciveFalse In application, the "preclusiveness" or "coerciveness" inquiry under Unocal/Unitrin and the inquiry into the board's "primary purpose" under *Blasius*, are not easily separable.[67]

There is evidence that the argument finding equivalency could fail on several grounds. First, the "preclusiveness" inquiry cannot be dissociated from other aspects of the *Unocal* standard, namely that the test provides a much lower exculpatory threshold for defendants to meet. Although judges are called upon to apply each component of the test separately, the agglomerated application of each component of the test could allow for an application that abstracts the whole into each discrete part. The primary purpose of interfering with the shareholder franchise is a potent judicial instrument. In several instances, the court of chancery faulted this inquiry for presuming a result as opposed to scrutinizing board action with the deference consistent with *DGCL* §141. But the "preclusiveness" inquiry, conducted within the context of allowing for a "legitimate corporate objective," severally waters down the principle that board action taken with the primary subjective mindset of interfering with the shareholder franchise should be invalidated absent a compelling justification. Secondly, taken together, the above two points may make a *Unocal* inquiry normatively different from a standalone *Blasius* inquiry. In this sense, an application of *Blasius* today would not necessarily produce the same effects as it did in *Chesapeake.*

67 Allen et al., *supra* note 45, at 887.

B. A SAB could withstand scrutiny of the reformulated Blasius *test under Unocal/Unitrin*

Even if the *Unocal/Unitrin* standard of review may be effectively equivalent to *Blasius*, an application of *Unocal* to a *Chesapeake*-like factual situation may present difficulties.

First, such a factual situation may arise without a "contest for control" scenario and the board could argue that there is no threat "touching upon issues of control" and therefore *Unocal* does not apply. A board wishing to enact a SAB will feel less constrained without the pressure of proxy advisory firms and institutional investors, which will vote such a proposal down. In such a case, *Unocal* scrutiny could simply prove inapplicable. By contrast, the pre-*Mercier Blasius* test requires no such threat. Although the primary purpose of interference would in all likelihood arise in response to a catalytic event, it by no means necessitates one.

Second, following *Unocal*, the board could be facing a threat in a *Chesapeake*-like factual situation and appear uprooted from a contest for control scenario. It could then argue that a SAB was enacted in good faith, served a legitimate corporate objective, and was reasonable and proportionate in relation to a threat—as the defendants did in *Chesapeake*. However, the findings of the court in *Chesapeake* then turned on a particular set of factual circumstances, which we discuss below.

1. Problems with Reasonableness

In *Chesapeake*, the court found that the defendants had responded to a legitimate threat by seeking a more adequate price for the shareholders. The defense only failed the reasonableness test on the grounds that the risk of confusion to the shareholder franchise was an inadequate threat. The court noted the following facts in support of its finding: the sophistication of institutional investors, which comprised 80% of the shareholder base; the number of analysts covering the stock; the extent of disclosure informing the shareholders of the transaction; the opportunity the defendants had to "address the confusion" through additional disclosure; the reputation of the company on Wall Street; and finally, the board's failure to conduct "any sort of informal survey" of its shareholders to see if confusion existed. On the face of this situation, it is not difficult to imagine an alternative set of facts that would support a legitimate assessment of shareholder confusion. Shorewood was a major company and most publicly listed companies will not necessarily share its same profile.[68]

[68] *See* Chesapeake Corp. v. Shore, 771 A.2d 293, 332 (Del. Ch. 2000).

The defense's argument in *Chesapeake* that the SAB was adopted to protect the shareholder franchise from the risk of confusion only failed due to factual deficiencies; it was an otherwise legally sound defense that could save a SAB. As the defendants submitted in *Chesapeake*: where the target board's decision to set an early and unannounced record date disenfranchised some holders and created confusion among others but would not "preclude" nor "substantially interfere" with a stockholder-bidder's consent solicitation to remove the target board, *Blasius* was "unwarranted."[69] And as proponents of SABs will argue, SABs can effectively serve the shareholder franchise.

2. Problems with Proportionality

In regards to the proportionality test, several facts persuaded the court to determine that the SAB was an "extremely aggressive and overreaching response to a very mild threat"[70] and "obviously preclusive." Shorewood already had a poison pill in place, it had adopted, contemporaneously with the SAB, a series of defensive bylaws which included the removal of the stockholders' right to call a special meeting, and the board exercised a considerable degree of control on procedures, including the setting of the record date. Taken together, these facts made the case for proportionality difficult to meet. But more importantly, the court found that the Supermajority Amendment threshold made it virtually impossible for the plaintiffs to win approval from Shorewood stockholders. As Vice Chancellor Strine colorfully put it with respect to the proportion of disinterested stockholder votes required to approve a bylaw amendment:

> the Supermajority Bylaw requires Chesapeake to obtain far higher than a majority—or 60% or 66 2/3%—of the disinterested votes. The required disinterested majorities are more commonly associated with sham elections in dictatorships than contested elections in genuine republics.[71]

As the court found, Shorewood's board adopted a Supermajority Bylaw that could only be surmounted by obtaining more than 88% of the disinterested votes, assuming a 90% turnout.[72] For all intents and purposes, the SAB made it mathematically impossible to defeat the board's position. Another distinguishing fact of this case is that Shorewood insiders collectively owned about 24% of Shorewoods' outstanding shares. The defendant's own expert witness, with

---

[69] *See id.* at 80. Vice Chancellor Strine refers to: *Golden Cycle*, mem. op. at 17; *H.F. Ahmanson & Co.*, mem. op. at 39-41 (saying that the delay of fifty days in holding meeting did not "impede the effective exercise" of franchise and therefore did not trigger *Blasius*; for same reason, delay was neither "preclusive nor coercive" under *Unocal*).
[70] *Id.* at 343.
[71] *Id.* at 342.
[72] *See id.* at 344.

twenty-one years in the proxy solicitation business, could not identify a single instance where an insurgent had been able to obtain a 60% supermajority when opposed by a 20-24% management block.[73]

Altogether, the factual circumstances detailed above suggest that (a) a reasonable threat of shareholder confusion, in addition to (b) a barrier not "obviously preclusive" and erected by the SAB (contrary to what Vice Chancellor Strine deemed the Bylaw in *Chesapeake*) could otherwise have been saved under *Unocal*/*Unitrin*, however imbued by *Blasius*.

3. A SAB is not necessarily "obviously preclusive" and could thus be saved

Delaware case law requires that an impugned corporate decision must have a realistic chance of success[74] and must be sufficiently disenfranchising to be invalidated. Both of these elements are problematic for a SAB because the law is unclear as to what degrees of success and disenfranchisement would be sufficient to strike a SAB.

Interestingly, the logic of the Chesapeake decision runs counter to *Unitrin*, which arguably involved the board of directors effectively issuing itself a 28% voting block and which stands for the proposition that this was not necessarily preclusive. Vice Chancellor Strine recognized this in *Chesapeake* and found a way around it by saying that *Unitrin* did not make a conclusion on the matter. But the potential contradiction, which Hutchison called a "paragon of incoherence" when comparing *Unitrin* with *Liquid Audio*, is suggestive of a potential factual situation where increased voting thresholds could be not "obviously preclusive".[75]

A similar situation arose in *Liquid Audio*, where the board action was arguably not preclusive. The decision by the Supreme Court of Delaware represents Delaware's strongest endorsement of *Blasius,* as it applied both *Blasius* and *Unocal* after the Court of Chancery did not find for the plaintiffs in their action against the board's decision to change the size and composition of the board, in the context of a contemplated merger. Specifically, the Court of Chancery ruled that *Blasius* did not apply because the board's decision "did not impact the shareholder vote or the shareholder choices in any significant way." The court denied relief under *Unocal* because the board's decision was neither preclusive

---

[73] *See id.* at 337-340.
[74] *See id.* at 333. (Meeting their burden to show that the Supermajority Bylaw is not preclusive, the defendants must show, per *Unitrin*, that it is "realistically" attainable for shareholders to prevail in a consent solicitation to amend the Shore bylaws. Case law requires a sufficiently disenfranchising effect).
[75] *See* Hutchison, *supra* note 27, at 1189.

nor coercive and further was not outside the range of reasonableness.[76] The Supreme Court of Delaware did not reverse the Court of Chancery's finding under *Unocal,* but found that *Blasius* applied and voided the board's changes. Notably, it ruled that there was a primary purpose of interference undertaken without a compelling justification[77] and cited the case as a "paragon of when the compelling justification standard of *Blasius* must be applied.[78]

Having raised the prospect that a *Chesapeake*-like SAB could arguably withstand *Unocal*/*Unitrin* review, a further problem arises when we consider the narrowed scope of applicability for *Blasius*. Since *Blasius* was first affirmed, a series of decisions have exerted pressure to reduce the scope of applicability for *Blasius*. In *Stahl v. Apple Bancorp, Inc.,* the court held that *Blasius* was inapplicable when the board changed the date of an annual meeting that was not imminent and in a manner that did not preclude a dissident from electing its slate.[79] In *Kidsco Inc. v. Dinsmore*[80], *Unocal* was applied to a bylaw amendment that extended the minimum allowable time for calling a stockholder-initiated special meeting from 35 days to 60 days. However, it held that because the bylaw amendment was a defensive response to a hostile takeover bid, its validity must be determined under the *Unocal/Unitrin* standard, and the "compelling justification" standard called for by *Blasius* was not applicable. The decision supported the proposition that board action, when taken as a defensive measure against a hostile tender offer, coupled with a proxy contest, does not implicate the *Blasius* standard of review. *Chesapeake* made exception to this holding, as discussed above. However, several pronouncements by the chancery court continued to extend the thrust of the *Stahl* and *Kidsco* decisions. In practice, courts will not invoke *Blasius* when the effect of the board's action is not sufficiently disenfranchising.[81] In *In re Gaylord Container Corp. S'holders Litig*., the court of chancery declined to apply *Blasius* review to various corporate governance changes, including eliminating the ability of shareholders to call a special meeting or act by written consent.[82] This doctrinal line still holds today, most recently epitomized *In re Ebix, Inc. S'holder Litig.*, which involved an amendment delaying, potentially indefinitely, a special meeting of the shareholders.[83]

---

76 *See* MM Cos. v. Liquid Audio, Inc., 813 A.2d 1118, 1121 (Del. 2003).
77 *See id.* at 1132.
78 *Id.* at 1131.
79 *See generally* Stahl v. Apple Bancorp, Inc., 579 A.2d 1115 (Del. Ch. 1990). (Holding that Blasius was not triggered when the Apple Bancorp board, in response to a simultaneous tender offer and proxy contest, set the annual meeting date for later than it had originally planned).
80 *See generally* Kidsco Inc. v. Dinsmore, 674 A.2d 483 (Del. Ch. 1995).
81 *See* Kling, *supra* note 43.
82 *See* In re Gaylord Container Corp. Shareholders Litig., 753 A.2d 462, 486-88 (Del. Ch. 2000).
83 *See* In re Ebix Stockholder Litig., No. 8526-VCN, 2016 Del. Ch. LEXIS 5 (Del. Ch. Jan. 15, 2016)

C. *An opening to successfully argue that SABs do not invite a* Blasius *inquiry*

Even if *Blasius* were to apply on a standalone basis, as it arguably did in *Chesapeake*, the uncertain restriction of *Blasius* to cases of entrenchment, director elections, and control could provide an opening to a board of directors to successfully argue that SABs do not invite a *Blasius* inquiry. To be sure, a *Chesapeake*-like situation could be resolved the same way *Chesapeake* was, via a dual analysis under *Blasius* and *Unocal*, and *Unocal* may suffice. But this ignores the doctrinal sublimation of *Blasius* into *Unocal* that has since occurred. The SAB would have to be not merely preclusive but also demonstrably of a nature that entrenches the board or management. As Jacob Kling argued, *Blasius* will only have limited force in non-entrenchment cases, as a result of the alteration of the *Blasius* test in *Mercier*.[84] In *Chesapeake*, the SAB was of a completely egregious nature, as it made it mathematically impossible for dissidents to have their voice heard. The entrenchment of the bylaw was also predicated under a standalone *Blasius* analysis on the motives of the board. Vice Chancellor Strine found "ample evidence of entrenchment."[85] But as discussed above, it should not be difficult to envision a scenario where a SAB was enacted but made it only marginally more difficult for dissidents to exercise their power in relation to the power to amend bylaws. After all, there were findings of nonentrenchment in *Blasius* and *Kidsco*.[86]

The answer thus turns on whether a postponement of a vote on a transaction implemented by the board, as in *Mercier*, is akin to a SAB that is not "obviously preclusive." On this point, Delaware law generally has little to say except to recognize the uncertainty. As Vice Chancellor Strine wrote in *Chesapeake*:

> In the more typical case involving board actions touching upon the electoral process, the question of whether the board's actions are preclusive is usually hotly contested. . .The line between board actions that influence the electoral process in legitimate ways (e.g., delaying the election to provide more time for deliberations or to give the target board some reasonable breathing room to identify alternatives) and those that preclude effective stockholder action is not always luminous. Absent confessions of improper purpose, the most important evidence of

[84] *See* Kling, *supra* note 43.
[85] *See* Chesapeake Corp. v. Shore, 771 A.2d 293, 345 n.123 (Del. Ch. 2000).
[86] *Id.* at 321-22. (Citing Kidsco in that Because the court found that the target board was not motivated by entrenchment but by a legitimate desire to avoid stockholder confusion and to secure time to seek more favorable strategic alternatives, it could not have been said to have acted for the primary purpose of impairing or impeding the effective exercise of the franchise nor would its actions have that effect).

> what a board intended to do is often what effects its actions have.[87]

The board of directors, for example, could argue that a SAB was enacted for the purpose of upholding the stockholder franchise. In other words, by effectively increasing the participation rate necessary to effect change at the corporate level, the directors would be serving the interest of shareholders in much the same way a quorum sets minimum standards for change.

To hint at just how "hotly contested" a situation might be, consider the act of issuing voting stock, which dilutes existing shareholders in the face of an incipient shareholder challenge and vote. Delaware cases have upheld such action when the interference with the shareholder franchise is incidental to a legitimate business purpose. In *Glazer v. Zapata*, the court remarkably held that:

> [The principle in *Schnell* that "the subversion of corporate democracy by manipulation of corporate machinery will not be countenanced under Delaware law" and found in *Blasius*]. . .does not require that management refrain from issuing voting securities, and thereby diluting the voting strength of insurgent stockholders, during the pendency of a proxy contest, when the issuance legitimately has a primary purpose directed to the management of the corporation and its business. Thus, like most equity cases, resolution of issues of this sort are typically highly particularized; factual.[88]

Cases like *Glazer*[89] should illustrate that even applying potent legal principles like those in *Blasius* does not ensure the protection of the shareholder franchise. Such cases also suggest that shareholders seeking to defeat a SAB may face even greater considerations before litigating if they are armed only with the reformulated *Blasius* test, since it is closer to the business judgment rule than the original *Blasius* test.

---

87 *Id.* at 320.

88 *See* Glazer v. Zapata Corp., 658 A.2d 176, 186 (Del. Ch. 1993).

89 *See BBC Capital Market, Inc. v. Carver Bancorp, Inc.,* No. Civ.A. 17743, 2000 WL 33521113 (Del. Ch. Feb. 16, 2000). (Refusing to invalidate the votes of shares representing about 8.3% of the outstanding voting interests which had been issued to two allegedly friendly investors after the corporation was notified of a forthcoming proxy contest. The plaintiff shareholder submitted a *Blasius* claim and argued that the issuance was for the primary purpose of impeding its ability to win the contest. The court held that the facts were hotly contested and that it could not grant injunctive relief "where important questions of material fact turn on the credibility of witnesses, with a focus upon actions they did or did not take based upon their subjective intent." The court also cited harm to defendant's interest if the two investors were denied chance to vote. Plaintiff did not argue that the board's action was defensive and did not make a *Unocal* argument but this should not be taken to suggest that a *Unocal* claim would have had a greater likelihood of success).

In the final analysis, the discussion above raises the prospect that a SAB could withstand *Unocal* scrutiny. It is further unclear, post-*Mercier*, how exactly *Blasius* would be applied to deal with a SAB that is not "obviously preclusive", nonentrenching, or enacted in response to a reasonable threat of shareholder confusion or a threat of inadequate price.

Even if it seeks to accommodate an important role for *Blasius*, the *Unocal/Unitrin* inquiry presents challenges perforce of limits and uncertainties for shareholder plaintiffs to succeed with respect to SABs. Resolving the predicament could involve relegating *Blasius* to become dead letter, as some have advocated[90], which would remove uncertainty but may simultaneously necessitate a reinvigoration of the "preclusiveness" standard. Conversely, it may reinstate *Blasius*, as the cases equitably demand it. The next section turns to this point by suggesting a legitimate area where the *Blasius* principles may play an "emphatic and enduring critical role."

VII. A VOID IN SEARCH OF PRINCIPLE AND PRINCIPLES TO FILL A VOID

The task of bringing certainty to the legal treatment of SABs may involve unresolved questions about the allocation of power between shareholders and directors under Delaware law. As Chancellor Allen put it in *Blasius*, "A decision by the board to act for the primary purpose of preventing the effectiveness of a shareholder vote inevitably involves the question who, as between the principal and the agent, has authority with respect to a matter of internal corporate governance."[91] As previously discussed, the reformulated *Blasius* test represents a shift toward board centrism in Delaware, in line with directorial power enshrined in *DGCL* §141. It also represents a discomfort with the shareholder-friendly principles articulated by Chancellor Allen in *Blasius*. This section thus argues that as the Chancery Court is called upon to clarify the emphatic and enduring critical role for *Blasius* in cases involving the power to amend bylaws, the *Blasius* principles will be relevant in deciding whether the shareholder franchise will be protected against SABs. This shareholder primacy is, moreover, consistent with the openness of Delaware law as it concerns the power to amend bylaws.

A. Blasius *and SABs*

Who, as a matter of law, is entitled to amend bylaws is at first a function of the corporation's constating text. In some cases, there are bound to be limitations. Firstly, the articles may be silent as to who prevails in the event of concurrent powers and each constituent may amend the bylaws consecutively, effectively

---

[90] Stephen Bainbridge, "Let Blasius go the way of the Dodo" (8 January 2013), www.professorbainbridge.com/professorbainbridgecom/2013/01/let-blasius-go-the-way-of-the-dodo.html.

[91] Blasius Industries, Inc. v. Atlas Corp., 564 A. 2d 651, 659-60 (Del. Ch. 1988).

reversing each other. Secondly, there may be situations not yet tested that involve a SAB, as suggested in Part IV of this paper, that is neither preclusive, entrenching nor outside the range of reasonableness. More generally, a SAB could be upheld: because there may be the absence of a reasonable threat (which would not be necessary to trigger *Blasius* scrutiny); because it was enacted in good faith and for a legitimate corporate objective; and lastly, because *Blasius* may not be effective given uncertainties about the scope of applicability post-*Mercier*. Yet, in all these instances, the SAB could still undermine shareholder action. In my view, this constitutes a type of potential case where the *Blasius* principles—whether reformulated or independently applied—could re-emerge as a credible fiat to protect the shareholder franchise.

B. A power vacuum for shareholder primacy

In Delaware law, a vacuum exists in relation to who holds the power to amend bylaws. This vacuum may be filled by the shareholder primacy inherent in *Blasius*. Delaware corporate law is board-centric but the power to amend bylaws, concurrently shared between the board and the stockholders, represents one notable exception. As some have commented, the allocation of power between shareholders and directors represents a significant area of uncertainty in Delaware law.[92] On the one hand, *DGCL* §109(a) provides that the power to adopt, amend or repeal bylaws shall be in the stockholders entitled to vote.[93] On the other, the same section provides an exception:

> Notwithstanding the foregoing, any corporation may, in its certificate of incorporation, confer the power to adopt, amend or repeal bylaws upon the directors[. . .]. The fact that such power has been so conferred upon the directors [. . .] shall not divest the stockholders [. . .] of the power, nor limit their power to adopt, amend or repeal bylaws.[94]

Fundamentally, *DGCL* §109(a) embodies internal contradiction and uncertainty. More broadly, this represents tension with *DGCL* §141, which upholds the power of the directors to manage the affairs of the corporation as a matter of principle[95], a "cardinal precept" underlying Delaware's board-centrism.[96]

---

[92] *See, e.g.,* Stephen M. Bainbridge, Corporate law 18 (2nd ed. 2009). *See also* L. John Bird, *Stockholder and Corporate Board Bylaw Battles: Delaware Law and the Ability of a Corporate Board to Change or Overrule Stockholder Bylaw Amendment*s,11 U. Pa. Bus. L.J. 217, 217-236 (2009).

[93] DEL. CODE ANN. tit. 8, §109(a).

[94] *Id.*

[95] DEL. CODE ANN. tit. 8, §141.

[96] *See* CA, Inc. v. AFSCME Emples. Pension Plan, 953 A.2d 227, 233 n.6 (Del. 2008).

Judicial controversy could ostensibly arise in the context of a SAB if the board of directors unilaterally adopted, in good faith, a SAB that was arguably non-onerous. This adoption, pending a shareholder-initiated bylaw and vote that could repeal it, would be the object of a claim in litigation. As explained in the preceding parts of this paper, limits and uncertainties may set a high bar for the shareholder plaintiffs. Further, in the event that constating documents are ambiguous, the court will proceed with a statutory analysis. In *Centaur*, the court examined the validity of a supermajority voting requirement of 80% of outstanding voting rights in the context of an election of directors.[97] It ruled that the amendment bylaw was clear and unambiguous and therefore overcame the presumption of a simple majority of votes cast rule with respect to an election of directors, as held in *Standard Power & Light Corp*.[98] Two observations may be made as it pertains to SABs: (1) there is no such statutory presumption for SABs, as will be covered below in addressing the uncertainty of the authority to amend bylaws; and (2) even if the constating documents are clear and unambiguous about the power of the directors to amend bylaw amendment provisions specifically, the situation should provoke fundamental questions about the equitable validity of the unilaterally enacted SAB.

There are two distinctive characteristics as it pertains to the impugned validity of an amendment bylaw unilaterally adopted by a board of directors:

1. Uncertainty underlying the allocation of power to amend bylaws

As discussed above, the power to amend bylaws is recognized as an unsettled area of Delaware corporate law. Specifically, courts have yet to resolve the question of whether the power to amend bylaws requires not only nothing less than, but also nothing more than, a majority of stockholder voting power.[99] Likewise, there is significant uncertainty as to whether a shareholder adopted bylaw is made immune from repeal or modification by the board of directors in the absence of an explicitly controlling statute.[100] But more illustrative of the prevailing general uncertainty is the Court of Chancery decision in *Boilermakers Local 154 Retirement Fund v. Chevron Corp*. The court ruled that a board could, without the concurrence of the shareholders, adopt bylaw provisions that permitted the corporation to choose the forum in which a shareholder-initiated suit would be maintained.[101] As James Cox wrote in a recent paper, the decision implies a broader, more fundamental question: are there limits on the board of

---

97 *See generally* Centaur Partners, IV v. National Intergroup, Inc., 582 A.2d 923 (Del. 1990).

98 *Id.* at 927.

99 Stephen M. Gill, Kai Haakon E. Liekefett, & Leonard Wood, *Structural Defenses to Shareholder Activism*, 47 REV. SEC. & COMMODITIES REG. 151, 156 (2014).

100 *See* Bainbridge, *supra* note 92, at 18; *see also* Bird, *supra* note 92.

101 *See generally* Boilermakers Local 154 Retirement Fund v. Chevron Corp., 73 A.3d 934 (Del. Ch. 2013).

directors to act through the bylaws to alter the rights shareholders customarily enjoy?[102]

2. Amendment bylaws: Challenging the nexus-of-contracts entity

Second, an amendment bylaw represents a renegotiation of, or rather a challenge to, the nexus of contractual relations that is said to metaphorically form the corporation. To be sure, *DGCL* §109(a) vests in the shareholders a power to adopt, amend or repeal bylaws that is legally "sacrosanct", i.e., the power cannot be non-consensually eliminated or limited by anyone other than the legislature itself.[103] But §109(a) does not exist in a vacuum. It must be read together with *DGCL* §141(a). No such broad management power is statutorily allocated to the shareholders. It is further well-established that shareholders of a corporation subject to the *DGCL* may not directly manage the business and affairs of the corporation, at least not without specific authorization in either the statute or the certificate of incorporation.[104] But this ignores three important ways that amendment bylaws engage the limits of the corporate form. (These were more broadly highlighted by Cox in the context of forum-selection clauses in *Boilermakers*.)

First, if bylaws are contracts subject to principles of contract law, as they are held to be within a statutory framework[105], then it would be a perversion of a key covenant between shareholders and the corporation to say that shareholders have pre-consented to being impeded from fully exercising their voting rights by assigning the power to amend bylaws to a board of directors. As Cox argues, the nexus-of-contracts view fails to honor two bedrock requirements (binding intent and definitiveness) mandated by contract law and which apply to unilaterally adopted bylaws.[106] In this sense, unilaterally changing amendment procedures with a primary purpose of interfering with the shareholder franchise plainly constitute a fundamental renegotiation of the contract between shareholder and directors, and by extension, a renegotiation of the corporate nexus or the entity-

---

[102] James D. Cox, *Corporate Law and the Limits of Private Ordering*, 93 WASH U. L. REV. 257, 258 (2015).

[103] CA, Inc. v. AFSCME Emples. Pension Plan, 953 A.2d 227, 232 (Del. 2008).

[104] *See id.*

[105]

[T]he bylaws of a Delaware corporation constitute part of a binding broader contract among the directors, officers, and stockholders formed within the statutory framework of the DGCL. This contract is, by design, flexible and subject to change in the manner that the DGCL. . .[T]he DGCL spells out and that investors know about when they purchase stock in a Delaware corporation.

See Boilermakers Local 154 Ret. Fund v. Chevron Corp., 73 A.3d 934, 939 (Del. Ch. 2013).

[106] Cox, *supra* note 102.

specific corporate contract itself.[107] Second, a SAB unilaterally adopted would extend beyond the private sphere and legitimately invite public policy into judicial reasoning. As this paper suggests, SABs raise public policy concerns. Third, a unilaterally adopted SAB, if upheld, would confuse authority over governance with managerial authority; improperly incorporate the shareholder's governance rights into the authority granted to the board of directors by *DGCL* §141(a); and ultimately violate the principle that "agents whose interests may materially diverge from the interests of their principals should not have the power to unilaterally determine or materially vary the rules that govern those divergences of interests."[108] *Blasius* supports these three propositions in the specific context of unilaterally adopted SABs as a matter of appropriate judicial interpretation.

C. Blasius *to intersect with the heads of bylaw amendment powers*

Together, these two main characteristics open a way for the *Blasius* principles to exert themselves. To be sure, the *Blasius* principles and their policy rationale were invoked in *Centaur Partners* but yielded to the clear and unambiguous SAB in the context of director elections.[109] But the bylaws were not unilaterally adopted by the board in response to the specter of shareholder engagement. In *CA, Inc*., *Blasius* was referenced merely to identify a legitimate and protected interest, not to wield the principles as doctrinal swords. The decision can be read to hold that §141 trumps §109(a); but, the court explicitly wrote that its holding was case-specific. The court wrote, "[w]herever may be the location of the bright line that separates the shareholders' bylaw-making power under §109 from the

---

[107] Though sparsely used, the term "entity-specific" overlaps with the nexus of contractual relations theory. For definition of entity-specific contract, see *Sinchareonkul v. Fahnemann*, 2015 Del. Ch. LEXIS 17, at *16-18 (Del. Ch. Jan. 22, 2015). As Vice Chancellor Laster wrote:
"When evaluating corporate action for legal compliance, a court examines whether the action contravenes the entity-specific corporate contract. The components of that contract form a hierarchy, comprising from top to bottom (i) the Delaware General Corporation Law (the "DGCL"), (ii) the certificate of incorporation, and (iii) the bylaws.7 Each of the lower components of the contractual hierarchy must conform to the higher components. A bylaw that conflicts with the charter is void, as is a bylaw or charter provision that conflicts with the DGCL."

[108] *See* Cox, *supra* note 102, at 264 (seeing *Blasius* as supporting a reorientation of the principal-agent relationship and advocates broader reach for the principle developed in *Blasius*, though not explicitly in the context of SABs (citing Melvin Aron Eisenberg, *The Structure of Corporation Law*, 89 COLUM. L. REV. 1461, 1464 (1989)). *See also* Blasius Industries, Inc. v. Atlas Corp., 564 A.2d 651 (Del. Ch. 1988).

[109] *See* Centaur Partners, IV v. National Intergroup, Inc., 582 A.2d 923, 927 (Del. 1990) (There exists in Delaware 'a general policy against disenfranchisement.' . . . This policy is based upon the belief that 'the shareholder franchise is the ideological underpinning upon which the legitimacy of directorial power rests.'" (citing *Blasius Industries, Inc.*, 564 A.2d at 669, 659); *See also* Concord Fin. Group v. Tri-State Motor Transit Co., 567 A.2d 1, 5 (Del. Ch. 1989). Therefore, elevated voting requirements which purport to protect minority shareholders by disenfranchising the majority, must be clear and unambiguous.

directors' exclusive managerial authority under §141(a), the proposed bylaw at issue here does not invade the territory demarcated by §141(a)."[110]

This paper attempts to show that the "bright line" which apportions bylaw amendment powers to shareholders and directors remains unsettled in Delaware law[111] This line overlaps with the line described as "rarely bright" by the judges who wrote *Function Over Form,* which separates board actions that legitimately influence the election process from board action that illegitimately impedes the exercise of the stockholder franchise..[112] Looking ahead and into this overlay, the *Blasius* principles still have currency. It is worth repeating Chancellor Allen's holding in *Blasius*: legitimacy is the ideological underpinning upon which directorial power rests and directorial power, even if exercised within its rightful purview under *DGCL* §141, may not inequitably encroach on the shareholders' dominion over internal corporate governance.[113] The two reasons above open a wide field, perhaps unlike any other, where this directional underpinning and limiting influence can instill clarity in an area whose development calls for it.

VIII. CONCLUSION

The *Blasius* principles are here to stay unless more is done to constrain them. Delaware law has not clearly exhausted, repudiated, or hermetically restricted the notions that decisions by the board (authorized by *DGCL* §141 but otherwise inequitable) may not interfere with the shareholder franchise and its dominion over internal governance. If we accept that the shareholder franchise is the ideological underpinning upon which directorial power rests, then Delaware law can expect to engage with the limits of the nexus-of-contracts corporate entity, particularly as it touches on the power to amend bylaws and supermajority requirements adopted unilaterally. Unless courts more effectively cage it, *Blasius* will put up a worthy fight against the centripetal force around the axis of directorial power firmly planted in Delaware law.

---

110 CA, Inc. v. AFSCME Emples. Pension Plan, 953 A.2d 227, 234 n.14 (Del. 2008).

111 Recent developments suggest judicial decisions may resolve conflicts in the balance of power between shareholders and directors. *See* Frechter v. Zier, C.A. No. 12038-VCG, 2017 WL 345142 (Del. Ch. Jan. 24, 2017), ruling that a bylaw requiring a supermajority of shareholders to elect directors was inconsistent with the plain wording of *DGCL* § 141(k) which states that "any director or the entire board of directors *may* be removed, with or without cause, by the holders of a majority of the shares then entitled to vote at an election of directors" (emphasis added).

112 Allen et al., *supra* note 45, at 1314.

113 *See* Blasius Industries, Inc. v. Atlas Corp., 564 A. 2d 651 (Del. Ch. 1988).