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# **ANALYSIS OF THE 1997 AMENDMENTS <sup>TO</sup> THE DELAWARE GENERAL CORPORATION LAW**

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## ANALYSIS OF THE 1997 AMENDMENTS TO THE DELAWARE GENERAL CORPORATION LAW

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### INTRODUCTION

The Delaware General Corporation Law was amended in 1997 for the eighth consecutive year. The 139th General Assembly approved a single bill that made changes to eleven sections of the statute. Many of the 1997 changes may be characterized as technical changes or as fine tuning or clarification of the existing law. There were, however, significant substantive changes in the provisions regarding indemnification, stockholder action by written consent and domestication of Delaware corporations into other jurisdictions. All of the changes in these areas were meant to increase the flexibility available to Delaware corporations and their advisors.

This article describes the changes effected by the 1997 amendments and supplements previous reports published by Aspen Law & Business and its predecessor, Prentice Hall Law & Business, describing amendments to the Delaware General Corporation Law.<sup>1</sup>

### FORMATION

**Contents of certificate of incorporation [§ 102].**—Section 102 governs the contents of the certificate of incorporation that must be filed with the Delaware Secretary of State in order to form a Delaware corporation. Section 102(a)(1) establishes specific requirements for the name of a Delaware corporation (such as the requirement, under certain cir-

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1. Arsht and Stapleton: Analysis of the New Delaware Corporation Law; Analysis of the 1967 Amendments to the Delaware Corporation Law; Analysis of the 1969 Amendments to the Delaware Corporation Law; Analysis of the 1970 Amendments to the Delaware Corporation Law; Arsht and Black: Analysis of the 1973 Amendments to the Delaware Corporation Law; Analysis of the 1974 Amendments to the Delaware Corporation Law; Analysis of the 1976 Amendments to the Delaware Corporation Law; Black and Sparks: Analysis of the 1981 Amendments to the Delaware Corporation Law; Analysis of the 1983 Amendments to the Delaware Corporation Law; Analysis of the 1984 Amendments to the Delaware Corporation Law; Analysis of the 1985 Amendments to the Delaware Corporation Law; Analysis of the 1986 Amendments to the Delaware Corporation Law; Analysis of the 1987 Amendments to the Delaware Corporation Law; Analysis of the 1988 Amendments to the Delaware General Corporation Law; Analysis of the 1990 Amendments to the Delaware General Corporation Law; Analysis of the 1991 Amendments to the Delaware General Corporation Law; Analysis of the 1992 Amendments to the Delaware General Corporation Law; Analysis of the 1993 Amendments to the Delaware General Corporation Law, Black & Alexander: Analysis of the 1994 Amendments to the Delaware General Corporation Law; Analysis of the 1995 Amendments to the Delaware Corporation Law; Analysis of the 1996 Amendments to the Delaware Corporation Law (Prentice Hall, Inc., 1967, 1969, 1970, 1973, 1974, 1976, 1981, 1983, 1984, 1985, 1986, 1987, 1988, 1990, 1991, 1992 and 1993, Aspen Law & Business, 1994, 1995 and 1996, respectively).

The 1997 amendments also make changes in subsections (c), (d) and (e) of Section 145 designed to distinguish indemnification and advances against expenses for officers and directors from indemnification and advances for employees and agents. Section 145(c), which mandates indemnification where the person seeking indemnification has been successful in defense of an action for which the statute authorizes indemnification, has been amended to apply only to directors and officers. Section 145(d), which provides that indemnification decisions are to be made by directors, legal counsel or stockholders, has been limited to indemnification decisions with respect to directors and officers. Section 145(e) has been amended to provide that the authorization to advance expenses to employees and agents need not be made at the board level. All of these changes recognize that decisions whether to indemnify or advance expenses for employees and agents are, for the most part, ordinary business decisions that, in contrast to such decisions with respect to directors and officers, do not have significant corporate governance implications. As a consequence, these decisions may be made at the general counsel level or by some other officer as part of the ordinary and routine business of the corporation.

### MEETINGS, ELECTIONS, VOTING AND NOTICE

**Meetings of stockholders [§ 211].**—Section 211 of the General Corporation Law requires that a corporation hold an annual meeting of stockholders for the election of directors and that if such an election is not held within thirty days of the date designated, or within thirteen months of the most recent annual meeting, stockholders may apply to the Court of Chancery for a summary order requiring that such a meeting be convened. Until recently, it was an open question whether the right of stockholders to act by written consent pursuant to Section 228 of the General Corporation Law could serve as a substitute for the annual meeting. Most practitioners believed, at least in the case of corporations whose shares are not publicly traded, that it was indeed permissible to obtain stockholder consent in lieu of holding an annual meeting. However, in 1996, in a case involving a minority stockholder of a private corporation, the Court of Chancery held that action by less-than-unanimous written consent could not replace a formal annual meeting at which stockholders have the opportunity to take part. See *TSI v. Hoschett*, 683 A.2d 43 (1996). It is important to note that the *Hoschett* Court limited its holdings to non-unanimous action, so that the decision does not apply to wholly-owned subsidiaries or to other corporations where unanimous written consent can be obtained.

The 1997 amendments to Section 211 respond to the *Hoschett* decision. First, Section 211 has been amended to make it clear that unanimous written consent to the election of directors can serve as a substitute for the annual meeting process. Furthermore, as amended, the statute provides that less-than-unanimous written consent electing directors in lieu of an annual meeting is permissible, but only if all the directorships to which directors could be elected at an annual meeting held at the effective time of the written consent are vacant and are filled by such action. This somewhat awkward-sounding requirement was intended to prevent insurgent stockholders from usurping the board's role in establishing orderly corporate governance procedures. Without the requirement that the directorships to be filled be vacant when filled, dissidents might attempt to use the written consent process to avoid the effect of staggered boards or provisions requir-

cumstances, that the name include a corporate indicator such as “Inc.” or “Corp.”). The 1997 amendments codify what is already a current practice of the Secretary of State, namely the regulation of the use of the word “bank” in a Delaware corporation’s name in order to avoid confusion and to protect the public interest. The new clause (iii) of Section 102(a)(1) provides that a corporation’s name cannot contain the word “bank,” or any variation thereof, unless the corporation is (1) under the supervision of the Delaware Bank Commissioner, (2) a subsidiary of a “bank” or “savings association” as those terms are defined in the Federal Deposit Insurance Act, or (3) a corporation regulated under the Bank Holding Company Act of 1956 or the Homeowners’ Loan Act. The amendment goes on to provide that the new clause (iii) should not to be construed to prevent the use of the word “bank”, or any variation thereof, if it is used in a context that clearly does not refer to a banking business and that would not otherwise be likely to mislead the public about the nature of the business of the corporation or that would harm the public interest. The Division of Corporations is given power to make that judgment.

### REGISTERED OFFICE AND REGISTERED AGENT

**Registered agent in State; resident agent [§ 132].**—A Delaware corporation must have a registered agent in Delaware for a number of purposes, including receipt of service of process, delivery of stockholder written consents and stockholder demands for inspection of corporate books and records. See 8 *Del. C.* §§ 220 & 228. Section 132 of the General Corporation Law contains the operative language requiring a corporation to have such a registered agent at its registered office within Delaware. The 1997 amendments clarify that the registered agent may be either the corporation itself, an individual resident in Delaware, or a domestic or foreign corporation authorized to transact business in Delaware, and that in each case such registered agent must have a business office that is generally open during normal business hours to accept service of process and to otherwise perform the functions of a registered agent. The purpose of this amendment is, in part, to foreclose any attempt to establish a registered agent businesses in Delaware by using a mail drop or other artificial addresses.

### DIRECTORS AND OFFICERS

**Indemnification of officers, directors, employees and agents; insurance [§ 145].**—Section 145 of the General Corporation Law authorizes a Delaware corporation to indemnify and advance expenses to directors, officers, employees and agents in a broad variety of circumstances and, in addition, requires such indemnification in a much narrower class of circumstances. It is, not surprisingly, one of the most closely studied provisions of the statute. Prior to the 1997 amendments, Section 145(d) provided generally that determinations with respect to a person’s entitlement to indemnification are to be made either by a majority of the directors who are not parties to the action for which indemnification is sought (even if less than a quorum) or by independent legal counsel or the stockholders. The 1997 amendments provide that, in addition, indemnification decisions may be made by a committee of one or more of the disinterested directors if the committee is designated by a majority vote of the disinterested directors.

appeared in Section 281. This amendment conforms Section 281 to the other statutory provisions relevant to liquidation, namely Sections 278, 280 and 282, and clarifies that Section 281 was not intended to prohibit the distribution of assets in kind to stockholders following dissolution of a corporation.

## FOREIGN CORPORATIONS

**Change of registered agent [§ 377].**—Section 377(b) prescribes the method by which a registered agent for a foreign corporation qualified to do business in Delaware may resign. The 1997 amendments revised the procedure by requiring that the registered agent give thirty days prior notice to the foreign corporation, and eliminating the requirement that the Secretary of State give notice to the foreign corporation of such resignation.

## DOMESTICATION AND TRANSFER

**Transfer and continuance of domestic corporations [§ 390].**—In 1995, the General Corporation Law was amended to establish a procedure, under Section 390, that permitted corporations to transfer from Delaware to a jurisdiction outside the United States. Among other things, the new provision enabled Delaware corporations to move to jurisdictions that did not recognize the concept of a reincorporation merger (which, within the United States, is the conventional method by which corporations change their domicile). The original 1995 version of the statute provided that, upon transfer out of Delaware, the corporation would cease to exist as a Delaware corporation.

In the ensuing two years, practitioners found that a number of beneficial transactions involving the movement of a Delaware corporation to a non-U.S. jurisdiction could not be consummated unless the corporation could, in addition to establishing its new domicile, retain its Delaware domicile. In order to provide the needed flexibility to accomplish such transactions, the 1997 amendments provide that in addition to a “transfer”, which involves leaving Delaware for the new jurisdiction, corporations may “continue” or “domesticate,” which words denote a domiciliation in the new jurisdiction without ceasing to exist as a Delaware corporation. Thus, under the amended statute, a corporation that follows the proper procedures may file a certificate of transfer, after which time the corporation will cease to exist as a Delaware corporation but will, for purposes of Delaware law, be considered to have transferred to the new jurisdiction. On the other hand, the statute now also provides that a corporation may file a certificate of continuance and thereafter, as a matter of Delaware law, continue both in the new jurisdiction and in Delaware.

The amendments to Section 390 raise novel issues. Corporations have, from time to time, attempted to establish “dual incorporation” status. For example, there have been a number of instances where non-U.S. corporations domesticated to Delaware under Section 388 of the General Corporation Law, which permits such corporations to domesticate into Delaware. Some such corporations have also continued their existence in the non-U.S. jurisdiction and thereby attempted to create such a dual status. Practitioners designing such transactions have determined that the theoretical uncertainties raised by one entity’s internal corporate structure being governed by two statutory schemes are



ing a high vote for removal of directors. While this resolution of the issues dealt with in *Hoschett* gives rise to cumbersome drafting, as a practical matter it gives corporations the latitude to dispense with an annual meeting by using written consents where there are no impediments to that course of action.

## MERGER OR CONSOLIDATION

**Merger or consolidation of domestic corporation and joint stock or other association [§ 254].**—Sections 251 through 258 and Sections 263 and 264 of the General Corporation Law provide for the merger or consolidation of Delaware corporations with a variety of domestic and foreign entities. In particular, Section 254 permits Delaware corporations to merge with joint stock associations and certain unincorporated associations, trusts and enterprises, including such entities formed under the laws of other jurisdictions. The 1997 amendments conform Section 254 to the other merger provisions authorizing mergers with non-Delaware entities by requiring that any non-Delaware entity surviving such a merger must appoint the Secretary of State of Delaware as its agent for service of process following the merger or consolidation.

**Appraisal rights [§ 262].**—Section 262 provides that in certain mergers, stockholders are entitled, after complying with the procedures set forth in the statute, to petition the Court of Chancery for an appraisal of the fair value of their shares. Section 262(b) provides that appraisal rights are not available in certain circumstances. This exception is commonly known as the “market out” and is generally applicable to the shares of a constituent corporation when both (1) the shares are listed or widely-held (as described in the statute) and (2) the holders of the shares are not required, pursuant to the agreement of merger, to accept anything for their shares other than shares of the surviving corporation, listed or widely-held shares, or cash in lieu of fractional shares, or any combination of the foregoing. The statute was amended in 1994 to provide that listed or widely-held depository receipts would be sufficient to meet *either* the first or second prong market-out exception, even if the underlying shares of stock were not listed or widely-held. The 1997 amendments clarify that the market-out is available even if depository receipts are used to satisfy *both* prongs (1) and (2) of the test.

## SALES OF ASSETS, DISSOLUTION AND WINDING UP

**Payment of franchise taxes before dissolution or merger [§ 277].**—Before a corporation may dissolve or merge out of existence, it is required, pursuant to Section 277, to pay all franchise taxes due. It has been the practice of the Secretary of State to calculate such franchise taxes through the entire calendar month during which the dissolution or merger becomes effective. The 1997 amendments codify this practice.

**Payment and distribution to claimants and stockholders [§ 281].**—Section 281(a) sets forth the procedures under which a dissolved Delaware corporation is to distribute its assets whenever it has followed the notice and claim procedures established by Section 280. Section 281(b) establishes the payment procedures applicable where a dissolved corporation has not followed such procedures. The 1997 amendments substitute the word “assets” for the word “funds” in each place where the latter word previously

outweighed by the business advantages that the structures provide. The 1997 amendments to Section 390, however, provide the first legislative recognition in Delaware of the validity of such dual status entities.

It is important to note that any transfer under Section 390 must be approved by all of the stockholders of the corporation. As a consequence, the section's principal utility has, in practice, been to permit corporations to move wholly-owned subsidiaries to foreign jurisdictions.

### **MISCELLANEOUS PROVISIONS**

**Taxes and fees payable to the Secretary of State upon filing certificate or other paper [§ 391].**—The General Corporation Law previously provided that reservations of corporate names made by telephone were subject to a \$10 fee, but that mail or hand delivery reservations were not subject to a fee. The 1997 amendments make all such reservations subject to a \$10 fee. In addition, Section 391 was amended to provide that certificates of continuance would require the same fee as certificates of transfer.

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