



DELAWARE SUPREME COURT INVALIDATES BYLAW AMENDMENT ATTEMPTING TO UNDERMINE THE EFFECT OF A STAGGERED BOARD IN A HOSTILE TAKEOVER

On November 23, 2010, the Delaware Supreme Court invalidated the amendment of a company's bylaws, the adoption of which would change the date of the company's annual meeting in an apparent attempt to circumvent the effect of a staggered board in an attempted corporate takeover. The case, *Airgas, Inc. v. Air Products & Chemicals, Inc.*, 2010 WL 4734305 (Del. Supr. Nov. 23, 2010), overturned the Delaware Court of Chancery's decision to the contrary, *Airgas, Inc. v. Air Products & Chemicals, Inc.*, No 5813-CC, 2010 3960599 (Del. Ch. Oct. 8, 2010). The Delaware Supreme Court held that the bylaw amendment, adopted at the annual meeting by the shareholders, was invalid since it was inconsistent with the Court's interpretation of Airgas, Inc.'s ("Airgas") charter requiring that each class of director serve three year terms.

The *Airgas* case arose from Air Products & Chemicals, Inc.'s ("Air Products") attempted takeover of its competitor Airgas. After Air Products launched a tender offer for Airgas and Airgas rejected several bids from Air Products, Air Products commenced a proxy contest at the annual meeting of Airgas held in September 2010. Since Airgas has a staggered board with nine directors, three positions on Airgas' board were up for election at the annual meeting. Air Products nominated three directors to the open positions on Airgas' board, all of whom were then elected by the shareholders. In addition, Air Products proposed a bylaw amendment (the "January Bylaw") that would schedule Airgas' next annual meeting only four months later (from September to January of the following calendar year). The January Bylaw also passed by a majority, 51.8%, of the votes cast by shareholders, but which constituted 45.8% of the shares entitled to vote. As a result, the January Bylaw had the effect of abridging the term of the three board of directors that would be up for election at the 2011 annual meeting by approximately eight months. The January Bylaw, in effect, undermined the purpose of a staggered board, which generally enhances the bargaining power of the target's board and makes it more difficult for an acquirer to gain control of its target, by potentially permitting Air Products to take control of the board of directors in four months, rather than in a year. Airgas followed by filing suit to declare the January Bylaw invalid.

The Court of Chancery concluded that Airgas' charter language regarding the duration of the directors' terms was ambiguous. The Court of Chancery went on to find that amendment was properly adopted at the annual meeting, did not conflict with Airgas' charter and was valid under Delaware law, and held the January Bylaw was a valid amendment. The lower court determined that January Bylaw was consistent because although it moved the annual meeting merely four months after the last annual meeting, it would occur in the next calendar year, which was not inconsistent with the ambiguous charter language.

The Supreme Court of Delaware, reviewing the decision *de novo*, agreed that the charter language defining the duration of the directors' terms was ambiguous, but noting the "overwhelming extrinsic evidence" concluded a term of three years was intended. According to the court, "because the January Bylaw prematurely terminates the Airgas directors' terms,



conferred by the charter and the statute, by eight months, the January Bylaw is invalid.”¹ In reaching its conclusion, the Supreme Court examined Airgas’ long-standing annual meeting practice, widespread corporate practice of Fortune 500 companies, the charter and bylaw language regarding the annual meeting term, the bylaw language regarding duration of directors’ terms and the charter provision requiring 67% of the voting power entitled to vote in order to alter, amend, or repeal Airgas’ staggered board position, or adopt any bylaw inconsistent with that provision. Since the “January Bylaw so extremely truncates the directors’ term as to constitute a *de facto* removal that is inconsistent with” Airgas’ charter, the Court held it invalid as it impermissibly shortened the three year staggered terms of the board positions and amounted to a *de facto* removal without cause of those directors without an affirmative vote of 67% of the voting power of Airgas as provided in its charter.²

Noting that while the three year term did not need to be measured with “mathematical precision,” or for them to “define with exactitude the parameters of what deviation from 365 days (multiplied by 3) satisfied the Airgas Charter three year durational requirement,” but in this specific case “we may safely conclude that under any construction ‘annual’ within the intended meaning of the Airgas Charter, four months does not qualify.”³

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¹ *Airgas*, at *1.

² *Airgas*, at *9.

³ *Airgas*, at *9.



Remember that these legal principles may change and vary widely in their application to specific factual circumstances. You should consult with counsel about your individual circumstances. For further information regarding these issues, contact:

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