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RECENT AMENDMENTS TO THE DELAWARE GENERAL CORPORATION LAW

On April 10, 2009, the Delaware legislature enacted amendments to the Delaware General Corporation Law ("DGCL") concerning stockholder participation in the corporate governance process. The amendments become effective August 1, 2009. Generally, the enacted amendments:

- Permit bylaws that require corporations to allow stockholders greater access to the corporation's proxy solicitations in order to nominate directors;
- Permit bylaws that require corporations to reimburse stockholders for proxy solicitation expenses in connection with director nominations;
- Prohibit charter or bylaw amendments that eliminate pre-existing rights to indemnification or the advancement of expenses for directors and officers after the acts or omissions that gave rise to the right to indemnification or advancement have occurred;
- Separate the record date for determining the stockholders entitled to notice of a stockholders' meeting from the record date for determining the stockholders entitled to vote at the meeting; and
- Allow, in limited circumstances, judicial removal of a corporation's directors.

New Section 112: Stockholder Access to Proxy Solicitation Materials

Section 112 of the DGCL allows, but does not require, a Delaware corporation to adopt a bylaw requiring any proxy solicitation materials circulated by the corporation regarding the election of directors to include nominees submitted by stockholders in addition to management's nominees.

Section 112 does not require stockholder access to proxy solicitations. Rather, it permits the corporation to adopt a bylaw to provide for such access. If such a bylaw is adopted, the requirement to include stockholder candidates in the

corporation's proxy material could be made subject to procedures and conditions such as those described below or any other lawful condition.

New Section 112 provides a nonexclusive list of permitted conditions and procedures, including:

- Requiring minimum record or beneficial stock ownership or minimum duration of stock ownership by the nominating stockholder;
- Requiring that the nominating stockholder provide specified information about the stockholder and the nominee, including information concerning stock ownership by both;
- Conditioning eligibility to require inclusion in the corporation's proxy materials upon the number or proportion of directors nominated by stockholders or whether the stockholders previously sought to require inclusion;
- Precluding nominations by a person if such person, any nominee of such person, or any affiliate of such person or nominee has acquired or publicly proposed to acquire shares constituting a specified percentage of the voting power of the corporation within a specified period before the election of directors; and
- Requiring that the nominating stockholder indemnify the corporation in respect of any loss arising from any false or misleading information or statement submitted by the nominating stockholder in connection with the nomination.

In light of new Section 112, Delaware corporations may wish to consider amending their bylaws to impose permitted restrictions on the availability of stockholder access to proxy solicitations with a view to preempting broader bylaw proposals by stockholders.

New Section 113: Stockholder Proxy Expense Reimbursement

Section 113 of the DGCL was enacted in response to the Delaware Supreme Court's decision in *CA, Inc. v. AFSCME Employees Pension Plan*.[1] At issue in that case was the validity of a stockholder proposal to amend the corporation's bylaws to require stockholder reimbursement for proxy solicitation expenses related to a short-slate election,[2] without giving any "fiduciary out" to the board of directors.

The Supreme Court held that a stockholder bylaw amendment proposal that, in general, provides for reimbursement by a corporation to a stockholder for proxy expenses relating to a short-slate election is a valid proposal and does not conflict with the board's right to manage the business and affairs of the corporation. However, the court held that the proposal in question was invalid because it did not provide the board sufficient flexibility to fully discharge its fiduciary duties to the corporation and its stockholders, should the board have believed the expenses not appropriate for the corporation (a fiduciary out).

[1] 953 A.2d 227 (Del. 2008).

[2] A short-slate election is where an insurgent stockholder nominates less than a majority of the registrant's board of directors.

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Section 113 of the DGCL authorizes a corporation to adopt a bylaw such as the one at issue in *CA, Inc*., which did not include a fiduciary out. Although the proposed amendment is silent with respect to a directors' fiduciary out, it is possible a Delaware court could read a fiduciary out into a bylaw enacted pursuant to Section 113.

The reimbursement right authorized by new Section 113 could be made subject to certain procedures and conditions including:

- Conditioning the eligibility for proxy expense reimbursement on the number or proportion of nominees sought to be elected by the stockholder so that reimbursement could only be available for short-slate elections;
- Limiting the amount of the reimbursement sought based on the relative success of the stockholder's nominees in the election or the amount incurred by the corporation in soliciting proxies for the same election;
- Limiting reimbursement for elections by cumulative voting; or
- Any other lawful condition.

Further, to prevent stockholders from claiming reimbursement for an election prior to enactment, Section 113 prohibits the application of any bylaw requiring reimbursement to any election for which the record date of the election precedes the adoption of the bylaw.

Directors of Delaware corporations may wish to consider amending their bylaws to impose restrictions on the availability of reimbursement for proxy solicitations regarding director elections with a view to preempting broader bylaw proposals by stockholders.

Section 145(f): Prohibition on Retroactive Elimination of Indemnification or Advancement of Expenses

The amendment to Section 145(f) is in response to the Delaware Chancery Court's decision, in *Schoon v. Troy Corp*.,[3] which upheld a bylaw amendment that eliminated the corporation's pre-existing bylaw commitment to advance expenses to a former director.

In some circumstances, the indemnification of directors and officers of Delaware corporations is mandatory. In *Schoon*, the court found that whether a corporation must indemnify or advance expenses to its decision makers does not depend on the charter or bylaws at the time the alleged cause of action arises, but rather what is set forth when legal proceedings are commenced against the director or officer on the cause of action. The *Schoon* decision has been rightly criticized for being unfair to directors and officers by allowing a corporation, after the fact, to terminate indemnification and expense advancement provisions in charters and bylaws which have been relied upon.

The amendment to Section 145(f) overturns *Schoon* by prohibiting amendments to a corporation's charter or bylaws that eliminate or impair rights to indemnification or advancement of expenses retroactive to the act or occurrence that gives rise to claims for indemnification or advancement. Under amended Section 145(f), a corporation could remove these

[3] 948 A.2d 1157 (Del. Ch. 2008).

director and officer protections after the time of the alleged wrongdoing only if the charter or bylaw provisions in effect at the time of the alleged wrongdoing expressly permitted retroactive elimination.

New Section 225(c): Judicial Removal of Directors

Section 225 of the DGCL permits the Delaware Court of Chancery to hear and determine the validity of any election, appointment, removal, or resignation of a director. New subsection 225(c) authorizes the Court of Chancery, upon application by the corporation or by a stockholder in a derivative suit, to remove a director who has been convicted of a felony or adjudged on the merits to have breached his or her fiduciary duty of loyalty to the corporation. The court could order removal if (a) it concludes that the director did not act in good faith when performing the actions that resulted in the felony conviction or judgment and (b) the action for judicial removal were brought subsequent to the underlying criminal or civil proceeding.

A corporation or stockholder seeking removal of a director must satisfy multiple procedural and evidentiary burdens. Although this amendment may run counter to the general principle that directors, who are elected by stockholders, should be removable only by the stockholders, other states have recently enacted statutory provisions allowing the judicial removal of directors as a means of removing “bad actor” decision makers when a stockholder vote would be futile. As the leading state for establishing best practices in corporate law, however, Delaware’s enactment of Section 225(c) may signify a movement toward greater deference to minority stockholder protections against malfeasant directors.

Amended Section 213(a): Separation of Record Dates

Under current Delaware law, a corporation’s board must set a record date for determining stockholders entitled **to notice and to vote** at a meeting between 10 and 60 days prior to such meeting. Under newly amended Section 213(a), the required record date for determining stockholders entitled to notice of a meeting would generally continue to be between 10 and 60 days prior to the meeting. However, the board now has the discretion of fixing a separate record date for determining stockholders entitled to vote on any date before, or even the day of, the meeting of the stockholders. By allowing the board to fix a record date for determination of stockholders entitled to vote at the meeting closer to the meeting date, the statute may reduce the potential for voting by persons who no longer have an economic interest in the stock.

The amendment to Section 213(a) also necessitated corresponding technical amendments to a number of other provisions of the DGCL, namely sections 211, 219, 222, 228, 262, and 275, to make them consistent with the allowance for separate record dates.

Conclusion

Under the direction of newly appointed Chairman Mary Shapiro, the Securities and Exchange Commission (“SEC”) staff has reportedly begun drafting new proxy access rules. The recent DGCL amendments may signal the beginning of the

states' response to perceived expansion of federal regulation in the proxy access arena. In developing proxy strategies, registrants should heed these new DGCL amendments as well as future SEC action.

– *Richard P. Wolfe* and *Peter J. Rivas*

SEC ADOPTS XBRL FOR FINANCIAL REPORTING

In an effort to assist investors in analyzing financial information, the SEC recently adopted rules requiring issuers to file a new exhibit to their SEC filings reproducing their financial statements, schedules, and footnotes in a data-tagged interactive format known as XBRL (eXtensible Business Reporting Language). With XBRL, investors will be able to download financial statement information directly into spreadsheets and analyze it using commercial off-the-shelf software, facilitating the comparison of financial and business performance across companies, reporting periods, and industries. For a copy of the final rule release, click here.

Compliance Schedule

This new XBRL exhibit will supplement, not replace, the SEC's current financial statement reporting requirements and will apply to annual and quarterly reports, transition reports, and registration statements that include financial statements (as well as any report on Form 8-K or 6-K that contains revised or updated financial statements). The XBRL requirements will apply to domestic and foreign public issuers that prepare their financial statements in accordance with U.S. Generally Accepted Accounting Principles ("GAAP") and foreign private issuers that prepare their financial statements using International Financial Reporting Standards ("IFRS"). The phase-in of XBRL for all public companies will take place in the following three stages over the next several years:

- Beginning with their quarterly or annual reports for the periods ending on or after June 15, 2009, large accelerated filers (domestic and foreign) that use U.S. GAAP and have a public float above $5 billion will be required to file XBRL reports.
- Beginning with the first fiscal period ending on or after June 15, 2010, all other large accelerated filers (domestic and foreign) that use U.S. GAAP will be required to file XBRL reports.
- Beginning with the first fiscal period ending on or after June 15, 2011, all remaining filers using U.S. GAAP or IFRS will be required to file XBRL reports.

During an issuer's first year of mandatory compliance, the face of the issuer's financial statements will be required to be tagged in detail (*i.e.,* each line item description and amount presented on the face of the financials must be tagged), and the financial statement footnotes and financial statement schedules will only need to be tagged as a single block of text. In the second year of mandatory compliance and thereafter, issuers will be required to specifically tag the detailed quantitative disclosures within the financial statement schedules and financial statement footnotes and may, in their discretion, also tag each narrative disclosure.

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The new rules contain a grace period for an issuer's first XBRL report, allowing an issuer up to 30 days from the earlier of date that it files its periodic report or the date the report is due to file its first XBRL report. Issuers taking advantage of the grace period will file the new exhibit as an amendment to the original filing. Similarly, the new rules provide for a 30-day grace period for an issuer's first XBRL filing that includes detailed tagging of financial statement footnotes and schedules.

Website Posting

In addition to filing XBRL-tagged financial statements with the SEC, issuers will be required to post the XBRL-tagged financial statements on their websites not later than the end of the calendar day the related report or registration statement is filed or is required to be filed, whichever is earlier. Notwithstanding the foregoing, the new rules contain 30-day grace periods for both an issuer's initial interactive data exhibit and the first interactive data exhibit that includes detailed tagging of financial statement schedules and footnotes. All interactive data posted on an issuer's website must remain on the site for at least 12 months.

Liability

For the first two years of an issuer's required XBRL reporting, interactive data exhibits will be deemed "furnished" and not "filed" for purposes of the liability provisions of the federal securities laws. Further, the XBRL files will be protected from liability for failure to comply with the tagging requirements if the failure occurs despite the issuer's good faith effort and the issuer corrects the failure promptly after becoming aware of it. Additionally, XBRL files will be excluded from the officer certification requirements of Rules 13a-14 and 15d-14 of the Exchange Act.

Failure to Timely File or Post

An issuer that fails to timely file or post to its website the required XBRL exhibit will be deemed not current with respect to its Exchange Act reports and, as a result, will be ineligible to use short form registration statements (such as Forms S-3 and S-8). Similarly, an issuer failing to timely file or post the XBRL report will also not be deemed to have available adequate current public information for purposes of Rule 144. However, once an issuer files the required XBRL exhibit, it will regain the ability to use short form registration statements and re-acquire current status for purposes of determining the adequate current public information required under Rule 144.

Voluntary Compliance

An issuer may, in its discretion, voluntarily comply with the XBRL rules prior to its compliance deadline. However, such an issuer must follow the same requirements as those mandated and can only use the 30-day grace periods for the initial submission and the initial detail-tagged-footnote submission, whether submitted voluntarily or required by the new rules.

– *Kelly C. Simoneaux* and *Allen E. Frederic*

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SEC ISSUES PROPOSED RULE—A "ROADMAP" FOR USE OF FINANCIAL STATEMENTS PREPARED IN ACCORDANCE WITH INTERNATIONAL FINANCIAL REPORTING STANDARDS ("IFRS")

The SEC has proposed a "Roadmap" to require U.S. issuers to convert from U.S. Generally Accepted Accounting Principles ("GAAP") to International Financial Reporting Standards ("IFRS") as the basis for financial reporting. The Roadmap contemplates a gradual transition from voluntary adoption by select companies (as early as filings to be made in 2010) to mandated use by all U.S. issuers (in annual reports for fiscal years ending on or after December 15, 2016). The SEC intends to determine in 2011 whether mandating adoption of IFRS is in the public interest.

Motivated by the increasing globalization of capital markets and a corresponding increase in international investment opportunities for U.S. investors, the SEC believes that a single set of global accounting standards is key to enhancing the ability of U.S. investors to compare financial information for U.S. and non-U.S. companies. Among other considerations, the SEC's decision whether to mandate use of IFRS will be ultimately based on the achievement of the following four milestones:

- Improvements in accounting standards. The issuers of GAAP and IFRS (the U.S. Financial Accounting Standards Board, "FASB," and the International Accounting Standards Board, "IASB," respectively) have been working together since 2002 toward the goal of a common set of high quality global standards, and the SEC will consider the degree of progress made by FASB and IASB towards this goal. The SEC will analyze such factors as whether the IFRS standards are of sufficient quality and breadth, and whether the development process is sufficiently robust, independent, and responsive to the views of affected parties, emerging economic issues, and changing business practices. With the stated goal of improving the accuracy and effectiveness of financial reporting, the SEC will evaluate the continued likelihood of the IFRS and converged GAAP-IFRS standards meeting these criteria.
- Accountability and funding of the IASC Foundation. Among the SEC's concerns regarding the adoption of IFRS is the IASB's lack of both regulatory oversight and a stable funding source. While the FASB is overseen by an organization which in turn is overseen by the SEC (the Financial Accounting Foundation, "FAF"), the IASB is currently overseen only by the IASC Foundation, a stand-alone, not-for-profit organization. The IASC Foundation seeks to establish a Monitoring Group comprised of national securities authorities from countries using its standards, including the SEC. The SEC assumes that this Monitoring Group will be established and functional by the time it considers mandatory use of IFRS, and will evaluate the effectiveness of that oversight prior to mandating use of IFRS. Additionally, the IASC Foundation is currently funded through voluntary contributions. The SEC considers the IASC Foundation's attainment of a stable funding mechanism that supports its independent functioning a prerequisite to any mandate of IFRS use.
- Improvement in the ability to use interactive data for IFRS reporting. The SEC has adopted rules requiring companies to provide financial data to the SEC and on the web in interactive data format using the eXtensible Business Reporting Language ("XBRL"). Given that a list of tags for interactive data reporting through XBRL has

been developed in greater detail for GAAP than for IFRS, the SEC will consider the extent of development of IFRS taxonomies.

- Education and training. The SEC is concerned about IFRS's unfamiliarity to a wide range of parties—investors, accountants, auditors, and others involved in the preparation and use of financial statements. Prior to mandating the use of IFRS, the SEC will consider the then-current state of education, training, and general readiness for IFRS, paying particular attention to readiness of the U.S. investor. The SEC acknowledges that a main benefit of a single set of global accounting standard—the ability for an investor to compare financial statements for both U.S. and foreign issuers—can only be reaped if that investor understands the basis for the reported results.

In addition, key to the SEC's determination will be a continued progress towards use of IFRS as the single set of high-quality globally accepted accounting standards and the consistent application of IFRS across companies, industries, and countries.

The Roadmap would permit voluntary early adoption of IFRS beginning with fiscal years ending on or after December 15, 2009, for any company that is one of its industry's 20 largest worldwide (based on market capitalization) and whose industry uses IFRS predominantly. Any such company would be required to seek confirmation of its eligibility from the SEC in the form of a "letter of no objection," which would permit that company to be an early adopter of IFRS within three years of the letter's date. The Roadmap proposes amendments to the SEC's rules, regulations, and forms which, if adopted, would facilitate early adoption.

Should the SEC determine to adopt these rules as proposed, mandatory compliance would be phased in over three years. "Large accelerated filers" would be required to prepare their three years of audited financials in accordance with IFRS beginning with the annual report for the first fiscal year ending on or after December 15, 2014, "accelerated filers" would have until their annual report for the first fiscal year ending on or after December 15, 2015, to comply, and all other filers would be required to comply by their annual report for the first fiscal year ending on or after December 15, 2016. Therefore, large accelerated filers would need to have prepared IFRS statements for 2012 and 2013 to include with the Form 10-K for 2014.

Once the switch has occurred, U.S. issuers would need to reconcile IFRS to GAAP. The Roadmap proposes two possible methods of reconciliation. "Proposal A" would require a one-time audited reconciliation from certain GAAP financial statements to IFRS in the issuer's first annual report on Form 10-K using IFRS. Like Proposal A, "Proposal B" would require the one-time audited reconciliation but imposes additional, ongoing disclosure of certain supplemental unaudited GAAP financial information covering a three-year period. This annual disclosure, relating to all annual periods covered by the IFRS audited financial statements (usually the three most recent fiscal years), would reconcile balance sheets, income statements, cash flow statements, statements of changes in shareholders' equity, and statements of comprehensive income.

The notice-and-comment period for this proposed rule ended on April 20, 2009.

– *Dionne M. Rousseau* and *Hope M. Spencer*

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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