MEMORANDUM

TO: Council of the Section of Corporation Law

FROM: Citizens for a Pro-Business Delaware, Inc.[1]

DATE: September 30, 2016

RE: Amendment to 8 *Del. C.* § 226

INTRODUCTION

Section 226 of the Delaware General Corporation Law (the "DGCL") concerns proceedings in the Delaware Court of Chancery when a Delaware corporation is deadlocked. In our view, Section 226 as currently enacted (it has not relevantly been updated since 1967) has at least two related deficiencies. First, it does not give sufficient guidance to the Court as to the many potential remedies developed by courts and academics over the past decades for dealing with corporate deadlock. Second, it provides no guidance or restrictions on when the Court should use the extreme remedies of forced dissolution or sale.

A forced sale, particularly of a solvent, even profitable entity, can interrupt and sabotage growth. It can interfere with adding new clients or keeping existing

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[1] Citizens for a Pro-Business Delaware, Inc. was formed in light of the Court of Chancery's post-trial holding in *In re Shawe & Elting LLC*, 2015 WL 4874733 (Del. Ch. Aug. 13, 2015) (hereinafter *TransPerfect*), ordering a solvent and profitable company sold, to advocate on behalf of employees of TransPerfect Global, Inc. We understand that an interlocutory appeal of *TransPerfect* has been accepted and is pending before the Delaware Supreme Court.

ones. It can interfere with vendor relationships. It can cause retention or hiring problems as to employees, naturally worried that a sale to an outside third party could destroy the corporation's long-term prospects or even existence (*e.g.* acquisitions for break-up value or to eliminate a competitor).

Rushing to sell or dissolve a corporation is all the more unfortunate given the many other methods available to resolve the circumstances giving rise to deadlock. Specified in state statutes and discussed by academics, these other methods include appointing a provisional director (a remedy the DGCL makes available to close but ***not*** regular Delaware corporations and describes in some detail in Section 353), appointing a custodian to help the parties work through deadlock, and granting specific injunctive relief to pinpoint and resolve key disputes.

The proposed amendment to Section 226 (attached as Exhibit A) requires that, before a court can force a solvent Delaware corporation to be sold or dissolved, one or more less restrictive remedies be tried for a three-year 'work it out' period. Such a period matches a prior Delaware case[2] and the DGCL often prescribes waiting periods before using extreme remedies.[3] It also clarifies that the

[2] *Bentas v. Haseotes*, 2003 WL 1711856, at *3-4 (Del. Ch. Mar. 31, 2003) (appointing a custodian, then ultimately ordering a non-forced sale).

[3] *See* 8 *Del. C.* § 284(c) (two-year period after incorporation before proceeding revoking charter for nonuse of corporate powers); 203(a) (Delaware's business

Court has the power to appoint a provisional director for a Delaware non-close corporation in Section 226 deadlock situations, whether using or departing from the default definition of the role in Section 353.

This amendment provides greater stability and predictability to Delaware corporations and those considering incorporation in Delaware by ensuring that the Court will only force a sale or dissolution of a deadlocked but solvent corporation as a last resort.

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combination antitakeover statute – three years); 278 (three-year wind-up period for dissolved corporation).

BACKGROUND

A. Section 226 Has Not Relevantly Been Amended Since 1967.

Section 226 was originally enacted in 1949. At that time it applied only to deadlocks in electing directors. *Giuricich v. Emtrol Corp.*, 449 A.2d 232, 236 (Del. 1982). In such circumstances it empowered the Court of Chancery to appoint a receiver with "the power to continue the corporate business unless otherwise ordered by the Court." *Id.*

The statute was substantially amended in 1967 as part of that year's major revisions to the DGCL. 56 Del. Laws ch. 50 (1967). That amendment, almost 50 years ago, changed it (relevantly) to its present form.[4] As well as expanding the circumstances justifying the appointment of a custodian or receiver, this revision further emphasized the disfavored nature of a liquidation and distribution of assets. Paragraph (b) provides in relevant part that the authority of any custodian of a solvent corporation is "to continue the business of the corporation and not to liquidate its affairs and distribute its assets, except when the Court shall otherwise order" (or in certain cases involving business abandonment or close corporations).

[4] Subsection (c) was later added regarding charitable nonstock corporations. 77 Del. Laws ch. 253 (2010).

The statute now provides as follows:

> **§ 226 Appointment of custodian or receiver of corporation on deadlock or for other cause.**
>
> (a) The Court of Chancery, upon application of any stockholder, may appoint 1 or more persons to be custodians, and, if the corporation is insolvent, to be receivers, of and for any corporation when:
>
> > (1) At any meeting held for the election of directors the stockholders are so divided that they have failed to elect successors to directors whose terms have expired or would have expired upon qualification of their successors; or
> >
> > (2) The business of the corporation is suffering or is threatened with irreparable injury because the directors are so divided respecting the management of the affairs of the corporation that the required vote for action by the board of directors cannot be obtained and the stockholders are unable to terminate this division; or
> >
> > (3) The corporation has abandoned its business and has failed within a reasonable time to take steps to dissolve, liquidate or distribute its assets.
>
> (b) A custodian appointed under this section shall have all the powers and title of a receiver appointed under § 291 of this title, but the authority of the custodian is to continue the business of the corporation and not to liquidate its affairs and distribute its assets, except when the Court shall otherwise order and except in cases arising under subparagraph (a)(3) of this section or § 352(a)(2) of this title.
>
> (c) In the case of a charitable nonstock corporation, the applicant shall provide a copy of any application referred to in subsection (a) of this section to the Attorney General of the State of Delaware within one week of its filing with the Court of Chancery.

B. Delaware Statute Allows Appointing Provisional Directors To Remedy Deadlocks, But Only In Close Corporations.

When a Delaware close corporation is deadlocked, Section 352 allows the Court to appoint a provisional director. Section 353(c) defines that role.[5]

Sections 341 to 356 of the DGCL apply only to "close corporations". To qualify a Delaware corporation must so elect in its certificate of incorporation. 8 *Del. C.* § 342. As most corporations do not,[6] a Delaware corporation could be non-public with few shareholders yet still not subject to that section of the DGCL.

Thus, for non-close corporations Section 226 allows suits for deadlock but Delaware statute does not make the provisional director remedy available.

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[5] *See* 8 *Del. C.* § 353(c) ("A provisional director shall be an impartial person who is neither a stockholder nor a creditor of the corporation or of any subsidiary or affiliate of the corporation, and whose further qualifications, if any, may be determined by the Court of Chancery. A provisional director is not a receiver of the corporation and does not have the title and powers of a custodian or receiver appointed under §§ 226 and 291 of this title. A provisional director shall have all the rights and powers of a duly elected director of the corporation, including the right to notice of and to vote at meetings of directors, until such time as such person shall be removed by order of the Court of Chancery or by the holders of a majority of all shares then entitled to vote to elect directors or by the holders of two thirds of the shares of that class of voting shares which filed the application for appointment of a provisional director. A provisional director's compensation shall be determined by agreement between such person and the corporation subject to approval of the Court of Chancery, which may fix such person's compensation in the absence of agreement or in the event of disagreement between the provisional director and the corporation.").

[6] *See* 1 O'Neal & Thompson's Close Corps. and LLCs: Law and Practice § 1:29 (Rev. 3d ed.) (noting vast majority of eligible corporations do not so elect).

C. For A Delaware Corporation In Deadlock There Are Numerous Alternatives To Forced Dissolution Or Sale.

There are many remedies available for deadlock other than forced sale or dissolution. For example, an Illinois statute specifically lists many, including appointment of a "provisional director":

> (1) The performance, prohibition, alteration, or setting aside of any action of the corporation or of its shareholders, directors, or officers of or any other party to the proceedings;
> (2) The cancellation or alteration of any provision in the corporation's articles of incorporation or by-laws;
> (3) The removal from office of any director or officer;
> (4) The appointment of any individual as a director or officer;
> (5) An accounting with respect to any matter in dispute;
> (6) The appointment of a custodian to manage the business and affairs of the corporation to serve for the term and under the conditions prescribed by the court;
> (7) The appointment of a provisional director to serve for the term and under the conditions prescribed by the court;
> (8) The submission of the dispute to mediation or other forms of non-binding alternative dispute resolution;
> (9) The payment of dividends;
> (10) The award of damages to any aggrieved party;
> (11) The purchase by the corporation or one or more other shareholders of all, but not less than all, of the shares of the petitioning shareholder for their fair value and on the terms determined under subsection (e); or
> (12) The dissolution of the corporation if the court determines that no remedy specified in subdivisions (1) through (11) or other alternative remedy is sufficient to resolve the matters in dispute. In determining whether to dissolve the corporation, the court shall consider among other relevant evidence the financial condition of the corporation but may not refuse to dissolve the corporation solely because it has accumulated earnings or current operating profits.

805 Ill. Comp. Stat. Ann. 5/12.56(b). Many states have similar lists. *E.g.*, Ga. Code Ann. § 14-2-941(a); Mo. Ann. Stat. § 351.855; Mont. Code Ann. § 35-9-502(1); Or. Rev. Stat. Ann. § 60.952(2); S.C. Code Ann. § 33-18-410(a); Wis. Stat. Ann. § 180.1833(2)(a); Wyo. Stat. Ann. § 17-17-141(a); *cf.* Model Bus. Corp. Act Ann., Model Statutory Close Corp. Supplement, § 41 (1984) (listing alternative remedies) (hereinafter MBCA-CC).

Commentators have similarly advocated such statutes listing remedies. Harry J. Haynsworth, *The Effectiveness of Involuntary Dissolution Suits as a Remedy for Close Corporation Dissension*, 35 Clev. St. L. Rev. 25, 26, 89 (1987) (citing cases) (deadlock statute "should specify a laundry list of other types of relief"; "[S]tatutory provisions which specifically authorize relief other than dissolution greatly enhance the probability that a judge will order an effective remedy in close corporation dissension litigation."); William S. Hochstetler, *Statutory Needs of Close Corporations-an Empirical Study: Special Close Corporation Legislation or Flexible General Corporation Law?*, 10 J. Corp. L. 849, 979 (1985) (deadlock statute may not meet a corporation's need if "it does not provide other flexible remedies").

Even in the absence of such specific statutes, however, courts have held that the court has "the inherent power to order any legal or equitable relief that will remedy the dissension, with dissolution being the last resort." Haynsworth, *supra*

at 41 (citing cases); *Bontempo v. Lare*, 119 A.3d 791, 805-06 (Md. 2015) (statute authorizing court of equity to grant dissolution for oppressive conduct implicitly authorized "less drastic equitable remedies" to that "extreme" remedy, including requiring dissolution "at a specified future date, to become effective only in the event that the stockholders fail to resolve their differences prior to that date").

D. Commentators Advocate That Alternative Deadlock Remedies Not Be Limited To Close Corporations.

Commentators have advocated that alternative remedies to dissolution be available for all corporations, not just those that are non-public or elect close corporation status. Susanna M. Kim, *The Provisional Director Remedy for Corporate Deadlock: A Proposed Model Statute*, 60 Wash. & Lee L. Rev. 111, 168 (2003) (proposing a model provisional director statute not limited to close corporations); Hochstetler, *supra* at 980 (suggesting alternative deadlock remedies not be limited to a "defined class of close corporations").

Indeed, the very fact that Section 226 has made deadlock of a non-close corporation actionable in Delaware raises the issue of what remedies should be available. It is important that alternative ones be available to non-close corporations because granting dissolution as a remedy can "unduly tip[] the balance of power to minority shareholders" and allow them to "exercise retaliatory oppression". Steven C. Bahls, *Resolving Shareholder Dissension: Selection of the Appropriate Equitable Remedy*, 15 J. Corp. L. 285, 296 (1990); *see also*

Haynsworth, *supra* at 30 ("granting minority shareholders a right to force dissolution" gives them an "enhanced bargaining position" that can lead to "minority tyranny").

The circumstances triggering Section 226 (deadlock or abandonment of corporate business) typically would occur only in non-public corporations limited to a small number of stockholders like entities that can qualify as Delaware close corporations upon election.

E. Alternatives Are Advocated Due To The Extreme Nature Of The Forced Sale And Dissolution Remedies.

One of the reasons that alternative remedies are advocated by commentators and pushed by courts is that dissolution is viewed as an "extreme remedy." Kim, *supra* at 113 n.6 (citing 16A William Meade Fletcher, Fletcher Cyclopedia of the Law of Private Corporations § 8043 (perm. ed. rev. vol. 1995)); *see also* Haynsworth, *supra* at 89 ("close corporation relief statutes should be recast so that involuntary dissolution is specified to be the last resort remedy rather than the primary relief"); Bahls, *supra* at 306-07 (alternative equitable remedies considered "[b]ecause of the potential losses associated with liquidating a business and the difficulty in fashioning an appropriate buyout or partition order").

The Maryland Supreme Court has noted that a corporation's "existence and operation" affects many others aside from its stockholders, including

"management, employees, and customers," and that dissolution affects those parties as well. *Bontempo v. Lare*, 119 A.3d 791, 806-07 (Md. 2015).

Shareholders who "believe their corporation has a promising future" may not believe "dissolution or a forced buy-out is an acceptable solution" for reasons including loyalty to employees, strong views of company continuation, keeping younger family members involved, and time and energy already expended. Kim at 124; *see also* Bahls at 296-97 (public harm from dissolving going enterprise presumably inheres to "displaced employees, suppliers, and frequently, customers").

There are also many problems associated with attempting to get a fair price for selling stockholders in forced sales. *See* Bahls at 331-36. For example, minority shareholders can be forced to forfeit "their interest in the going concern premium of the business," valuing shares "is difficult and expensive," and buyout by the corporation can create "liquidity problems". *Id.* at 331, 334.

F. A Model Code And Many State Statutes Require A Court To Determine No Other Remedies Adequate Before Ordering Dissolution.

Many states have imposed additional restrictions on the drastic forced dissolution remedy. Illinois and Oregon require a court to determine that no "alternative remedy is sufficient to resolve the matters in dispute". 805 Ill. Comp. Stat. Ann. 5/12.56(b); Or. Rev. Stat. Ann. § 60.952(2)(m).

The ABA Model Statutory Close Corporation Supplement proposes, and six states have adopted with minor revisions, a substantially similar provision. MBCA-CC § 42 (If the court finds the listed alternative remedies "inadequate or inappropriate, it may order the corporation dissolved".); Ga. Code Ann. § 14-2-942; Mo. Ann. Stat. § 351.860(1); Mont. Code Ann. § 35-9-503(1); S.C. Code Ann. § 33-18-420(a); Wis. Stat. Ann. § 180.1833(2)(a)(9)-(10); Wyo. Stat. Ann. § 17-17-142(a).

G. The Provisional Director Remedy Offers Many Benefits To A Deadlocked Corporation.

"Part of the value of provisional directors lies in their ability to mediate between hostile factions and to encourage both sides to consider new ideas and alternatives for resolving disputes amicably." Kim, *supra* at 114. "The introduction of an outsider tends to put the parties on their best behavior." *Id.* at 135. For that reason, provisional directors can be akin to mediation. *Id.* at 134; Bahls, *supra* at 308-09 (calling such remedies "in effect, appointing in-house arbitrators"). Such a remedy, like others, often are effective also "because they give the bitterly disputing parties an opportunity to calm down for a period of time". Kim, *supra* at 124.

Appointing a provisional director is also more limited relief than appointing a custodian. For example, "having only one vote," the provisional director "cannot initiate actions over the objections of the other directors." Bahls, *supra* at 310.

H. *TransPerfect* Orders The Forced Sale Of A Deadlocked Solvent Corporation.

In *In re Shawe & Elting, LLC*, 2015 WL 4874733 (Del. Ch. Aug. 13, 2015)[7] (hereinafter *TransPerfect*), the Court of Chancery held that there were stockholder and director deadlocks under 8 *Del. C.* § 226(a)(1) and (a)(2). *Id.* at *1. The Court held that there were "essentially three alternatives available." *Id.* at *30-31. The Court rejected the first option to "decline to appoint a custodian and leave the parties to their own devices". *Id.* at *31.

The Court noted that a second option was "to appoint a custodian to serve as a third director or some form of tie-breaking mechanism in the governance of the Company". The Court rejected this on the reasoning that "it would enmesh an outsider and, by extension, the Court into matters of internal corporate governance for an extensive period of time." *Id.* The Court discussed that because the principal deadlocked parties were both "relatively young," their tenure as directors and co-CEOs could continue for decades. *Id.* The Court reasoned, "It is not sensible for the Court to exercise essentially perpetual oversight over the internal affairs of the Company." *Id.*

The Court did not further discuss the basis for, or extent of, its belief that it would be necessarily drawn into disputes regarding internal corporate governance.

[7] An interlocutory appeal of this decision has been accepted and is pending before the Delaware Supreme Court.

It did not seem to consider the fact that notwithstanding such objections a provisional director remedy for close corporations is allowable via statute. 8 *Del. C.* § 352. Nor did it consider the fact that provisional directors can be appointed for a limited time.

The Court determined to select the final option, "to appoint a custodian to sell the Company". *Id.* The Court cited only two Delaware cases in which it had ordered sales of profitable corporations, calling it "unusual". *Id.* at *31 & n.320. The Court conceded that in one of those cases the parties themselves had agreed on a dissolution remedy. *Id.* (citing *Fulk v. Wash. Svc. Assocs., Inc.*, 2002 WL 1402273 (Del. Ch. June 21, 2002)).

In the second, *Bentas v. Haseotes*, the Court initially appointed a custodian to cast a tie-breaking vote on significant disputes. 769 A.2d 70, 79 (Del. Ch. 2000). The Court rejected defendants' earlier argument that the custodian be directed to sell the company, directing the custodian instead to explore all alternatives that might result in a "mutually agreed solution" to the deadlock. *Id.* at 80. More than three years later, the deadlock had not been resolved, and the Court selected the custodian's and plaintiffs' proposal to auction the company over defendants' proposal to divide the company in half. *Bentas v. Haseotes*, 2003 WL 1711856, at *3-4 (Del. Ch. Mar. 31, 2003). The Court does not discuss any

argument that the company should not be sold or divided, only arguments over the way it should be sold or divided.

DISCUSSION

I. SECTION 226 SHOULD BE AMENDED TO REQUIRE ALTERNATIVE REMEDIES BEFORE DISSOLVING OR SELLING A SOLVENT CORPORATION.

The proposed amendment to DGCL Section 226 inserts the following language as subsection (d):

> (d) A custodian appointed pursuant to paragraphs (a)(1) or (a)(2) of this section shall not have the authority to dissolve or sell a solvent corporation unless necessary parties stipulate, or:
>
> > (1) The Court grants one or more alternative remedies to resolve the deadlock such as appointing a custodian, provisional director (as defined in Section 353 of this title or otherwise), or tie-breaker vote on the board, amending the bylaws or certificate of incorporation, or otherwise granting injunctive relief; and
> >
> > (2) After such remedies have been functioning for at least three years, the Court determines upon an evidentiary hearing that deadlock remains, no alternative remedy is sufficient to resolve the deadlock, and such corporation should be dissolved or sold.

Ex. A.

This amendment adds a requirement before the extreme remedy of dissolving or selling a solvent[8] corporation is available in a Section 226 deadlock case. The Court must grant one or more remedies other than dissolving or selling the corporation. There are many remedies a Court can choose from including but

[8] Delaware courts are of course well acquainted with the criteria for determining whether a corporation is solvent. *Quadrant Structured Prod. Co., Ltd. v. Vertin*, 115 A.3d 535, 556 (Del. Ch. 2015).

not limited to the ones named: appointing a provisional director or tie-breaker vote on the Board, amending the bylaws or certificate of incorporation, or granting other injunctive relief to surgically resolve specific sources of contention.

Such remedy must function for at least three years. This provides a 'work-it-out' period after deadlock has been found in which one or more remedies can be ordered, hopefully successfully. This is similar to the period of time in *Bentas* between the Court's decision appointing a custodian and the Court's decision on a motion to determine a plan of liquidation.

If the deadlock thereafter remains and no alternative is sufficient to resolve it, the Court then has the discretion to order dissolution or sale.

A. The Amendment Permits Appointing A Provisional Director, Previously Only Statutorily Available To Close Corporations.

This amendment clarifies Delaware law by expressly providing that a provisional director remedy is available for deadlock even in non-close corporations. As discussed above, *supra* at 6, Delaware statute only references a provisional director in deadlocks of corporation that elect close status. This amendment would allow the Court to appoint a provisional director using the default definitions contained in Section 353 or to depart from them in its discretion.

The DGCL makes a deadlock cause of action available to non-close corporations. 8 *Del. C.* § 226. Thus, it is only sensible that a potential deadlock

remedy, particularly one less extreme than forced sale or dissolution, be similarly open to non-close corporations. Kim, *supra* at 115; Hochstetler, *supra* at 978.

The Court has recently implied that it has the authority to appoint provisional directors for deadlocked non-close corporations. *See TransPerfect*, 2015 WL 4874733, at *31 (discussing as an "option" appointment of "a custodian to serve as a third director or some form of tie-breaking mechanism"); *but see Barry v. Full Mold Process, Inc.*, 1975 WL 1949, at *2 (Del. Ch. June 16, 1975) (denying provisional director request because corporation was not close). This amendment would confirm the Court has this remedial power.

B. The Amendment Requires And Partially Lists Remedies Other Than Dissolution Or Sale.

Another benefit of this amendment would be that it expressly calls to the Court's attention a range of options other than dissolution or sale with which to resolve deadlock. Commentators have advocated such statutes. Haynsworth, *supra* at 26, 89 ("[S]tatutory provisions which specifically authorize relief other than dissolution greatly enhance the probability that a judge will order an effective remedy in close corporation dissension litigation"; such "statutes should specify a laundry list of other types of relief that can be granted by a judge".); Hochstetler, *supra* at 979 (dissolution provisions may not meet a corporation's need if "it does not provide other flexible remedies").

C. A Three-Year 'Work-It-Out' Period Is Required Before A Solvent Delaware Corporation Is Ordered Dissolved Or Sold.

Before a solvent Delaware corporation is dissolved or sold for deadlock, the amendment requires the Court to grant one or more alternative remedies. The amendment sets up a 3-year 'work-it-out' period during which the parties can see if these remedies resolve the deadlock.

A solvent corporation has established mutually beneficial relationships with a web of interconnected persons, including employees, customers, and vendors. As set forth above, *supra* at 10-11, remedies of dissolution or sale are extreme because they significantly threaten or eliminate these mutually beneficial arrangements. So it is generally beneficial to see if less draconian remedies will succeed.

Of course, if a deadlock is sufficiently intractable such that the parties agree, they can stipulate to the entrance of such remedies without such a three-year period. Thus, the amendment only affects *involuntary* dissolutions and *forced* sales.

The three-year period is similar to the period of time in *Bentas* between the Court's decision appointing a custodian and the Court's decision on a motion to determine a plan of liquidation. *Bentas v. Haseotes*, 769 A.2d 70, 79 (Del. Ch. 2000); *Bentas v. Haseotes*, 2003 WL 1711856, at *3-4 (Del. Ch. Mar. 31, 2003). It also resembles a remedy suggested by the Maryland Supreme Court in *Bontempo*

v. Lare of an order requiring dissolution "at a specified future date, to become effective only in the event that the stockholders fail to resolve their differences prior to that date". 119 A.3d 791, 806 (Md. 2015).

A required waiting period before such a substantial action also has precedent in the DGCL. *See* 8 *Del. C.* §§ 284(c) (proceeding to revoke a corporation's charter for nonuse of corporate powers cannot be instituted within two years of incorporation), 203(a) (Delaware's business combination antitakeover statute prohibiting business combination with a person becoming a significant stockholder for three years absent board approval), 278 (dissolved or expired corporation must continue for three years to litigate lawsuits, pay off liabilities, and distribute assets). Each cited statute, like forced sales or dissolutions in Section 226, involve fundamental corporate changes.

This amendment requires a Court hearing before a forced sale or dissolution is granted, which only reflects the probable Court practice in a situation of such magnitude to a Delaware corporation. *See also* 8 *Del. C.* §§ 168(b) (Court may compel issuance of new stock certificate if satisfied with plaintiff's case "upon hearing"), 296(b) (Court may determine rights of creditor or claimant of insolvent corporation "after hearing").

The statute requires that the Court find no "alternative remedy is sufficient to resolve the matters in dispute". This provision is substantively identical to an

Illinois statute applicable to (as most deadlock proceedings concern) non-public corporations. 805 Ill. Comp. Stat. Ann. 5/12.56(b) (dissolution only allowable if "if the court determines that no . . . other alternative remedy is sufficient to resolve the matters in dispute"). As set forth above, *supra* at 11-12, the Model Statutory Close Corporation Supplement has proposed and many other states have adopted similar provisions.

D. This Amendment Will Benefit Delaware Solvent Corporations And The Public.

The clear benefit of this statute is that it requires the granting of some remedy less than dissolution or sale when a solvent corporation is deadlocked. Parties who have been so successful as to create a solvent, even profitable Delaware corporation are thus prompted to use a remedy other than dissolution or sale. It is to be hoped that this would vastly reduce if not eliminate the need for stronger remedies.

The concern has been expressed that appointing custodian to serve as a provisional director could result in additional Court involvement for "decades". *TransPerfect*, 2015 WL 4874733, at *31.

This amendment resolves any such concern. Under this provision, any resulting involvement would be statutorily limited to three years before stronger remedies are available. Moreover, at most this amendment only requires one

additional involvement point by the Court, that being a decision at the end of the three-year period that dissolution or sale is warranted.

It is also worth noting that Delaware has, notwithstanding this concern, made custodial relief expressly available by statute to remedy deadlocks in all corporations and the appointment of a provisional director available by statute to remedy deadlocks in close corporations.

Further details are subject to the Court's considerable equitable discretion in managing its cases. If it is concerned that a provisional director will engender dispute, it could appoint that person as a custodian as well to resolve certain disputes within the appropriate bounds of that custodian's role. It could also explore utilization of the Masters in Chancery or special masters. *See, e.g.*, *DiGiacobbe v. Sestak*, 743 A.2d 180, 182 (Del. 1999) (citing Chancery Court Rules 135-47 and 10 *Del. C.* § 372).

Delaware courts have used less intrusive remedies to resolve deadlock such as those initially required by this statute. See *Giuricich v. Emtrol Corp.*, 449 A.2d 232, 240 (Del. 1982) (appointing custodian to act where the board could not reach a unanimous decision, to call directors' or stockholders' meetings, and to serve as the Court deemed necessary absent unanimous shareholder request for discharge); *Niehenke v. Right O Way Trans., Inc.*, 1995 WL 767348, at *4 (Del. Ch. Dec. 28, 1995) (appointing custodian for one year "to resolve issues for which the directors

cannot reach a decision" and soliciting applications to extend such period); *Miller v. Miller*, 2009 WL 554920, at *5 (Del. Ch. Feb. 17, 2009) (appointing custodian for two years to break material director deadlocks, resolve "operational deadlocks," substitute as director under certain circumstances, and "seek to resolve the impasse over the future of the Company"). These cases demonstrate what kinds of alternative remedies Delaware courts have granted, and would consider under this amended statute, to resolve a deadlock. They also show that it is not uncommon for the Court to appoint a custodian for a lengthy period of time.

CONCLUSION

Section 226 should be amended to allow the Court of Chancery to dissolve or sell a solvent corporation only as a last resort after less intrusive alternatives have failed. The proposed amendment provides a non-exclusive list of alternatives the Court may consider while preserving the Court's flexibility to implement the most equitable and efficient remedy. It will benefit not only stockholders but also management, employees, and customers of Delaware corporations by providing additional stability and fairness to the process of dealing with deadlock.

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CONCLUSION

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Exhibit A

AN ACT TO AMEND TITLE 8 OF THE DELAWARE CODE RELATING TO THE GENERAL CORPORATION LAW.

BE IT ENACTED BY THE GENERAL ASSEMBLY OF THE STATE OF DELAWARE (Two-thirds of all members elected to each house thereof concurring therein):

Section 1. Amend § 226, Title 8 of the Delaware Code, by inserting a new subsection (d) as follows:

> "(d) A custodian appointed pursuant to paragraphs (a)(1) or (a)(2) of this section shall not have the authority to dissolve or sell a solvent corporation unless necessary parties stipulate; or:
>
> > (1) The Court grants one or more alternative remedies to resolve the deadlock such as appointing a custodian, provisional director (as defined in Section 353 of this title or otherwise), or tie-breaker vote on the board, amending the bylaws or certificate of incorporation, or otherwise granting injunctive relief; and
> >
> > (2) After such remedies have been functioning for at least three years, the Court determines upon an evidentiary hearing that deadlock remains, no alternative remedy is sufficient to resolve the deadlock, and such corporation should be dissolved or sold.

Ssynopsis

This bill's changes to the Delaware General Corporation Law are recommended by the Delaware State Bar Association.

Section 1. This amendment provides that the Court of Chancery may only appoint a custodian to dissolve or sell a solvent corporation to resolve deadlock if (1) alternative remedies prove insufficient after three years or (2) sufficient persons stipulate. It includes a non-exclusive list of deadlock remedies.