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Revisiting Your Corporate Bylaws — Now's the Time to Address the Changing Landscape

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A number of important regulatory, legislative and market developments over the last two years have made this an ideal time to revisit your corporate bylaws in order to determine whether changes should be made to reflect current law and best practices. These developments include changes that could have a significant impact on stockholder meetings and voting, such as regulatory changes related to discretionary voting by brokers and laws related to establishing record dates for notice of and voting at stockholder meetings. In addition, as a result of recent developments in Delaware law, corporations may want to consider adopting bylaws establishing Delaware as the exclusive forum for litigation. The following suggestions address some of the actions Delaware corporations should consider:

TREATMENT OF BROKER NON-VOTES AND ABSTENTIONS

On July 1, 2009, the Securities and Exchange Commission (the "SEC") approved an amendment to New York Stock Exchange Rule 452 that eliminated discretionary voting by brokers in uncontested director elections, effective January 1, 2010. Under revised Rule 452, brokers are no longer permitted to vote on behalf of a stockholder in any uncontested election for directors unless the broker receives voting instructions from the stockholder. In addition, under Section 957 of the Dodd-Frank Wall Street Reform and Consumer Protection Act (the "Dodd-Frank Act"), brokers are not only prohibited from voting for the election of directors without customer instruction, but they are also prohibited from voting without instruction on executive compensation matters, including advisory votes or any other significant matter (as determined by the SEC).

These recent regulatory and legislative changes give rise to important issues for public companies, which often have a significant number of shares held in "street name" by retail investors who regularly fail to instruct brokers as to how to vote their shares. When brokers do not have discretion to vote uninstructed shares on a particular proposal, the stockholder's failure to instruct the broker will result in a "broker non-vote". Under Delaware law, abstentions and broker non-votes are not shares authorized to vote and are not considered votes cast on a matter. However, if a corporation's bylaws contain an ambiguous voting standard or explicitly provide for a different treatment of abstentions and broker non-votes, any increase in broker non-votes, as a result of the recent regulatory changes, could have a significant impact on voting results.

Given the significant potential impact of broker non-votes on stockholder voting as a result of these regulatory changes, it is important for public companies to ensure that their voting standards are clear and unambiguous. Delaware public companies should review their bylaws and charter provisions to ensure that the impact of broker non-votes and abstentions on voting at stockholder meetings is clear. Without clear standards, public companies may face increased difficulties in determining whether a vote requirement has been met. We generally recommend that bylaws provide that: (i) except as otherwise required by law, the certificate of incorporation or the bylaws, all actions taken by the holders of a majority of the votes cast on a matter at a meeting at which a quorum is present shall be valid and binding upon the

corporation, except that adoption, amendment or repeal of bylaws by stockholders will require the vote of a majority of the shares entitled to vote, and (ii) broker non-votes and abstentions are considered for purposes of establishing a quorum but not considered as votes cast for or against a proposal or director nominee.

MAJORITY VOTING FOR DIRECTORS

Corporations should review their majority voting bylaws to ensure that they reflect current best practices. As a result of the regulatory changes described above with respect to broker discretionary voting, corporations should revisit their majority voting bylaws to ensure that they employ a clear voting standard that does not result in a broker non-vote being counted as a vote against a nominee. In addition, corporations that have adopted majority voting should ensure that their bylaws identify how to address directors receiving less than a majority of the votes cast in an election and whether a different voting standard should be used in contested elections.

RECORD DATES FOR STOCKHOLDER MEETINGS

Effective August 1, 2009, the Delaware legislature amended Section 213(a) of the Delaware General Corporation Law (the "DGCL"), related to setting record dates for those entitled to vote at stockholder meetings. Under the old statute, the same record date had to apply to both notice of a stockholder meeting and entitlement to vote at such meeting. If there is a long period of time between the record date and the meeting date, a significant number of stockholders of record as of the record date may sell their stock. As a result, many persons entitled to vote at the meeting will not actually own stock on the meeting date. This is sometimes referred to as "empty voting". Under amended Section 213(a), corporations are able to fix a separate record date for notice of a meeting and for voting at the meeting. The establishment of a second, later record date for voting at a meeting is meant to increase the likelihood that at the time of the meeting, more of the corporation's current stockholders are entitled to vote. The board of directors is under no obligation to establish separate record dates, and if only a single record date is set, that record date establishes both the right to notice and the right to vote.

Delaware corporations should review their bylaws and determine whether to amend their bylaws to permit the board of directors to establish separate record dates for notice of, and voting at, a meeting of stockholders. Publicly traded companies should keep in mind that they must continue to comply with federal securities laws, which, among other things, require the timely distribution of proxies to stockholders and which limit the applicability of this provision. However, the SEC has published a Concept Release in which it states that it is considering changes to its rules to provide for dual record dates. Although it has not issued any rules on this matter, these changes to Delaware law provide boards with more flexibility and Delaware corporations should consider relevant changes to their bylaws.

DELAWARE AS EXCLUSIVE FORUM

In a recent decision, the Delaware Chancery Court suggested in dicta that provisions in a Delaware corporation's charter documents that mandated that a particular forum be used for intra-entity disputes (including derivative actions) would be enforceable in Delaware. Revising a corporation's bylaws or charter to contain a forum selection clause could provide significant advantages to Delaware corporations. Delaware courts have substantial expertise and experience in matters of corporate law, and litigating matters of Delaware law in Delaware courts is generally viewed as more efficient and results in a more consistent application of Delaware law than litigating in other forums. Although it is not clear whether jurisdictions outside of Delaware will give effect to such provisions, Delaware corporations should seriously consider amending their bylaws and/or charter to provide that Delaware be the exclusive forum for intra-entity disputes.

STOCKHOLDER PROXY ACCESS FOR NOMINATION OF DIRECTOR CANDIDATES

On August 25, 2010, the SEC adopted rules providing stockholders with access to a corporation's proxy statement for the nomination of director candidates under certain circumstances, in the form of a new Rule 14a-11 (and other associated amendments) under the Exchange Act. The SEC subsequently stayed the effect of Rule 14a-11, pending resolution of litigation against the SEC brought by the Business Roundtable and the U.S. Chamber of Commerce in the US Court of Appeals for the District of Columbia. The timing for the court's review is unclear, and we are not recommending that corporations revise their bylaws to reflect the new proxy access rules until resolution of the litigation.

CONCLUSION

We recommend that Delaware corporations carefully review their bylaws in connection with their regular review of their governance practices. The impact of the above regulatory and legislative changes on their bylaws should be carefully considered as part of this review. Please feel free to contact Morrison & Foerster LLP if you need any assistance with evaluating your policies in light of new requirements, perspectives and best practices.

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