

Client Alert

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Delaware Supreme Court Upholds Advance Notice Bylaw

The Delaware Supreme Court recently held that a stockholder activist failed to comply with an advance notice bylaw. The Supreme Court ruled that the bylaw was clear and unambiguous and the activist's failure to comply rendered its nominees ineligible. In doing so, the Supreme Court reversed the Court of Chancery's determination that the board of directors had acted outside the scope of the advance notice bylaw by demanding supplemental information from the activist stockholder.

Background

BlackRock Credit Allocation Income Trust v. Saba Capital Master Fund, Ltd., involved two closed-end investment funds structured as Delaware statutory trusts. Under the funds' bylaws, a stockholder was required to provide advance notice of its intent to nominate directors at the funds' annual meetings. Importantly, the nominating stockholder was also required to supplement its notice with "any subsequent information reasonably requested by the Board of Directors to determine that the Proposed Nominee has met the director qualifications as set out in Section 1 of Article II [of the bylaws]." The supplement was due no later than five business days after being requested by the board of directors.

Last year, stockholder Saba Capital timely notified the funds of its intent to nominate directors at the funds' annual meetings. In response, the funds' outside counsel emailed Saba Capital a lengthy supplemental questionnaire seeking additional information about its nominees. The stockholder did not return the completed questionnaires within the five-business-day period. The funds consequently deemed the nominations improper under the bylaws.

The Court of Chancery held that the nominations could not be disregarded under the advance notice bylaws. It reasoned that the boards "went too far" by demanding information that was not reasonably requested or necessary to determine whether the nominees met the director qualifications set forth in the bylaws. "By including in the Questionnaire a substantial number of questions unrelated to Section 1's director qualifications, and nonetheless enforcing the strict five-day deadline to invalidate Saba's nominations," the court wrote, "Defendants overstepped their authority under Section 7(e)(ii) [of the bylaws] while demanding strict compliance from [the stockholder]." The funds appealed the Court of Chancery's ruling.

The Delaware Supreme Court's Ruling

On January 13, 2020, the Supreme Court reversed the lower court in favor of the funds. Writing for the court, Justice Karen Valihura held that the bylaws were clear and unambiguous in empowering the board to solicit additional information that had to be provided within five business days. "[W]e are reluctant," she wrote, "to hold that it is acceptable to simply let pass a clear and unambiguous deadline contained in an advance-notice bylaw, particularly one that had been adopted on a 'clear day.'" The court continued that:

A rule that would permit election-contest participants to ignore a clear deadline and then, without having raised any objection, proffer after-the-fact reasons for their non-compliance with it, would create uncertainty in the electoral setting. Encouraging such after-the-fact factual inquiries into missed deadlines could potentially frustrate the purpose of advance notice bylaws, which "are designed and function to permit orderly meetings and election

contests and to provide fair warning to the corporation so that it may have sufficient time to respond to shareholder nominations.”

Importantly, the Supreme Court observed that the stockholder admitted at least some of the requested information was within the board’s authority under the bylaw: “It is undisputed that at least one-third of the questions in the Questionnaire are directly relevant to Section 1” and “it is undisputed that Saba failed to respond in any way prior to the deadline.” Thus, the fact that some of the board’s demands fell outside the scope of the advance notice bylaw did not justify the stockholder’s complete failure to respond or timely object to the request.

Lastly, the Supreme Court rejected the stockholder’s argument that the boards had acted improperly. The court found no record of manipulative conduct and was unwilling to infer misconduct, even though the boards’ actions would foreclose a proxy contest.

Contact

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