

M&A Update

Delaware Chancery Court Invalidates Charter and Bylaw Provisions Allowing Only For Cause Removal of Directors Where Board is Not Classified

January 5, 2016

In a December 21, 2015 transcript ruling, the Delaware Chancery Court invalidated the provisions of VAALCO Energy, Inc.'s charter and bylaws that allow for removal of directors only "for cause" even though VAALCO's board is not classified. Vice Chancellor Laster ruled that the charter and bylaw provisions conflicted with the plain reading of Section 141(k) of the Delaware General Corporation Law, which states that stockholders may remove directors from the board with or without cause except where the board is classified or directors are elected by cumulative voting.

Background

Until its 2010 annual meeting, VAALCO had a classified board and its certificate of incorporation and bylaws provided that directors could be removed only for cause. Following the board declassification, the certificate of incorporation and bylaws continued to provide that directors could be removed from office only for cause. VAALCO investor Vladimir Gusinsky Living Trust brought the lawsuit challenging the removal clause in connection with a consent solicitation led by Group 42, Inc. seeking to remove four members of the VAALCO board of directors – representing a majority of the members of the board – without cause and replace them with four nominees of Group 42.

Takeaways

Although the decision is consistent with a prior Chancery Court interpretation of Section 141(k) (see *Rohe v. Reliance Training Network*, 2000 WL 1038190 (Del. Ch. July 12, 2000)), Vice Chancellor Laster's ruling makes clear how any ambiguity in a corporation's constituent documents around rights to remove directors will be resolved. The following are key takeaways from the ruling:

1. *Delaware Corporations Without Classified Boards That Have Provisions Limiting Removal of Directors to "For Cause" Only Should Be Aware that Their Charter or Bylaw Provisions May Be Similarly Invalid.* VAALCO noted that 175 Delaware corporations with

unclassified boards and no cumulative voting provide for removal of directors only “for cause,” and argued that an invalidation of the VAALCO provisions could have far reaching consequences for a multitude of companies. Vice Chancellor Laster found this argument unpersuasive. Accordingly, companies with similar provisions should consider their defensive profiles and be aware that their directors may be removed without cause in the event of a campaign by stockholders to replace some or all of the directors. Indeed, following the decision, VAALCO entered into a settlement agreement with Group 42, which resulted in significant changes to the VAALCO board. Consideration should also be given to what, if any, amendments to an affected company's charter or bylaws should be proposed, as well as what, if any, disclosure requirements arise as a result of the VAALCO ruling.

2. *Companies With Classified Boards Should Consider the Implications of the Ruling on Any Decision to Declassify Their Board.* The VAALCO Board was previously classified and the removal provision of the constituent documents was not revised in connection with the declassification. Companies that declassify should consider all applicable provisions when declassifying. In addition, while not ruling specifically on the issue, Vice Chancellor Laster left open the theoretical possibility that a company could declassify in a manner that preserved “for cause” removal only.
3. *Supermajority Requirements to Remove Directors Are Still Valid.* The ruling did not address charter or bylaw provisions providing that directors may only be removed by a supermajority vote of the shareholders. Delaware law provides wide latitude for companies to specify in their constituent documents higher voting requirements for corporate matters than those otherwise provided by law.

For a full copy of Vice Chancellor Laster's ruling, click [here](#).

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If you have any questions, please contact any of the following attorneys or your Cadwalader contact:

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