

Delaware Seeks to Avoid a “DExit” of Corporations

Corporate, Securities, and Governance



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Delaware Democratic Governor Matt Meyer signed a bill that significantly alters the corporate governance landscape, sparking debate among corporate leaders, institutional investors, and legal professionals.

The legislation is intended to reinforce Delaware's dominance as the legal home for corporations after the high-profile departures of several companies. However, it has also drawn criticism for allegedly favoring corporate insiders at the expense of investors.

Here's what in-house counsel need to know about the latest developments.

Why Delaware?

Delaware has long been a premier jurisdiction for incorporation, thanks to its sophisticated and business-friendly legal framework. The state is home to more than two million corporate entities, including two-thirds of Fortune 500 companies.

Delaware's Chancery Court has expertise in handling corporate cases. It also has a well-developed body of case law that provides predictability and efficiency in resolving business disputes.

This strong legal infrastructure has historically made Delaware the preferred choice for companies seeking stability and clarity in corporate governance. And being business-friendly is big business for Delaware: The state generates billions in revenue from corporation-related activities, funding nearly one-third of its operating budget.

Key provisions of the new law

The new law will:

- **Increase protections for corporate officers and controlling shareholders.** The bill makes it more difficult to bring lawsuits against controlling shareholders and officers in conflicts of interest cases.
- **Place stricter limits on document discovery.** The legislation curtails shareholders' ability to access corporate documents, potentially making it harder to prove corporate misconduct in court.

Legal challenges to the law are widely expected.

ACC Members-only Article: Proposed Amendments to Delaware General Corporation Law Aim to Clarify Corporate Transaction Rules

Recommendations for in-house counsel

Given these developments, corporate legal teams should take proactive measures to assess the impact of this legislation on their organizations. Key steps for in-house counsel include:

- **Reevaluate incorporation strategy.** Companies should reassess whether Delaware remains the optimal jurisdiction for their corporate structure or if alternative states provide rules that are more in line with their desired corporate approach.
- **Review governance and compliance policies.** With increased protections for executives, boards should ensure internal governance policies align with best practices and investor expectations.
- **Assess legal risk exposure.** In-house counsel should analyze how the reduced access to corporate documents may impact litigation risk and shareholder relations.
- **Monitor litigation trends.** Given the likelihood of legal challenges to the new law, staying informed about evolving case law will be critical for corporate legal teams.

1. Broader business and legal impact

In-house counsel — especially CLOs and those involved in business strategy discussions — may also want to consider the following questions as the corporate legal landscape evolves:

2. Impact on investor relations and capital raising

- How will institutional investors respond to these changes?
- Could Delaware's reduced transparency lead to higher capital costs for companies incorporated there?
- Will activist shareholders intensify scrutiny or seek alternative governance measures to compensate for reduced legal leverage?

3. Repercussions on M&A and corporate transactions

- Will the new legal landscape create complications in due diligence for M&A activity?
- Could limitations on document discovery impact deal-making and valuations?
- How should companies adjust their transaction strategies in response?

Competitive landscape of corporate jurisdictions

- How real is the threat of a "DExit" — as the exodus has been dubbed — and which jurisdictions offer the most viable alternatives if needed?
- What tax, legal, and governance trade-offs exist when considering incorporation in other jurisdictions, such as Nevada or Texas?
- Should companies proactively engage with Delaware officials or legal bodies to seek further clarifications or amendments?

4. Board-level risk and reputation management

- How should boards address potential backlash from institutional investors or proxy advisory firms?
- Does this create reputational risk that could affect a company's environmental, social, and governance (ESG) standings?
- What messaging, if any, should be developed to communicate with stakeholders regarding potential impacts of these amendments.

5. Legal exposure and compliance adjustments

- Should corporate legal teams implement new disclosure strategies or internal compliance measures?
- How do these changes impact whistleblower policies and internal investigations?
- What steps should companies take to protect against potential legal challenges related to conflicts of interest?

Staying vigilant in times of change

Delaware's new legislation represents a pivotal shift in corporate law, with significant implications for in-house counsel, boards, and shareholders. While the law aims to reinforce Delaware's corporate dominance, it has also raised questions about fairness, transparency, and long-term investor confidence. Legal teams must stay vigilant, adapt their strategies accordingly, and anticipate potential shifts in corporate governance dynamics.

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