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Litigators of the Week: The Delaware Supreme Court Turns Its Spotlight on Advance Notice Bylaws

By Ross Todd
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Last week the Delaware Supreme Court weighed in with what Bloomberg Law dubbed a "first-of-it-kind" ruling dealing with advance notice bylaws, a subject that has emerged as the latest legal tug-of-war between activist investors and corporate board.

Our Litigators of the Week are **Teresa Goody Guillén** and **Richard Raile** of **Baker & Hostetler** and **John Seaman** of **Abrams & Bayliss** who represent Ted Kellner, an AIM ImmunoTech Inc. stockholder who saw his nominations for board seats rejected under what the Delaware court called the company's "sweeping new advance notice provisions" adopted during an activist campaign requiring a trove of information about potential board nominees.

"In the middle of a proxy contest, the AIM board adopted one unintelligible bylaw and three unreasonable bylaws," Chief Justice Collins J. Seitz Jr. wrote. "The AIM board's motive was not to counter the threat of an uninformed vote. Rather, the board's primary purpose was to interfere with Kellner's nomination notice, reject his nominees, and maintain control."

The court found all the amended bylaws were the product of an improper motive and purpose, inequitable, and, therefore, unenforceable.



Courtesy photos

L-R: Teresa Goody Guillén & Richard Raile of Baker & Hostetler, and John Seaman of Abrams & Bayliss.

Lit Daily: Who is your client and what is at stake here?

Teresa Goody Guillén: Our client who is named in the lawsuit, Ted Kellner, is a successful businessman, generous philanthropist, and the second largest individual stockholder of AIM. There are two additional clients, Todd Deutsch and Robert Chioini. Mr. Deutsch is a successful businessman and the largest individual stockholder of AIM. Mr. Chioini is also a successful businessman, with particular expertise and passion in pharmaceuticals, especially cancer treatments. These three men, individually and collectively, stand up for what is right and just, even at a personal cost.

What is at stake is no less than corporate democracy and stockholders' sacrosanct rights. Stockholders own corporations, not the directors, and AIM's directors have rigged the corporate machinery such that stockholders don't have a choice other than the incumbents. AIM is a failing company, and our client and other stockholders have lost much of their investments at the hands of directors and a CEO who have presided over the company since 2016. Our client believes the company's leading pharmaceutical product, Ampligen, has value and potential, but the board of directors has failed to maximize that value while entrenching itself and, hence, lacks any incentive to improve shareholder value. Believing a proxy contest imminent, the board enacted expansive, draconian, and labyrinthian advance-notice bylaw disclosure rules with the purpose and effect of ensuring that there would be no contested election. The board then followed through by rejecting our client's nomination notice, which secured the members' reelection to the AIM board. So the question, simply put, was whether AIM stockholders should have the democratic choice to elect directors who will place the interests of the corporation and stockholders above their own interests. Stepping back, the question more generally is whether other boards may insulate themselves from stockholder will by similar means.

How did this matter come to you and your firms?

Goody Guillén: The BakerHostetler team and I were recommended to Mr. Kellner and Mr. Deutsch by one of their lawyers and Mr. Chioini. I have represented Mr. Chioini in other matters as well. Mr. Kellner and Mr. Deutsch were separately aware of us for our representation of another AIM stockholder. We hold Mr. Seaman in the highest of regards and knew that he and his Delaware colleagues would perfectly complement our team.

Who all has worked on this matter and how have you divided the work?

Goody Guillén: Besides Richard Raile and me, our team is comprised of the following BakerHostetler attorneys: **Marco Molina**, **John Harrington**, **Alexandra Trujillo**, **Ambika Singhal**, **Mike Neminski** and **Jeff Lyons**; as well as the following Abrams & Bayliss attorneys: John Seaman, **Elie Feinstein** and **Eric Veres**.

While some work is allocated based on logistical and practical considerations, we primarily divided the work strategically, based on the strengths and expertise of our lawyers. Notably, Mr. Raile was integrally involved in the trial level, but was more behind the scenes. Thus, he was well-steeped in the case from the beginning even though he did not make an appearance until the appellate stage.

The decision notes that "it is apparent that confusion existed in the Court of Chancery between a 'validity' challenge and an 'enforceability' challenge" to advance notice bylaw provisions under Delaware law. Was that a distinction you had tried to make below at the Chancery Court?

Richard Raile: We viewed the distinction between "validity" and "enforceability" (and "facial" and "as-applied" challenges) as a red herring meant to confuse the courts into believing they could not review the challenged bylaws under equitable principles. We did not introduce the issue; the defense did. Our strategy at the trial and appellate stages was, first and foremost, to focus the courts back onto the case law holding that bylaw amendments adopted in response to stockholder nominations are subject to enhanced judicial review for compliance with directors' fiduciary duties. The holding that the bylaws are "unenforceable" does as much for our client in this case as a holding that they are "invalid," and the courts at both levels properly reviewed the bylaws for adherence to the directors' duty of loyalty (which the Supreme Court

found violated). Accordingly, we view our strategy as a success.

What's important in this decision for investors such as your client seeking board seats in Delaware corporations?

John Seaman: The significance of the Delaware Supreme Court's opinion is that stockholders can be assured the Delaware courts will declare unenforceable expansive and overreaching advance notice bylaws implemented by directors motivated by preserving their power and control. While corporate advance notice bylaws remain valid tools to obtain information about stockholder nominees and their proposals to ensure an informed stockholder electorate, directors, management and their advisors cannot exaggerate the threat of an uninformed vote as a basis to extract unreasonable informational demands from stockholders. Advance notice bylaws that are designed to be "unintelligible" or function as a "tripwire" to reject nominations will be subject to enhanced scrutiny review and declared invalid or unenforceable unless the board justifies these requirements and proves it did not have the purpose of thwarting a proxy contest. The decision does not answer all questions related to advance notice bylaws and disclosure requirements, but it does warn boards to tread carefully, if nothing else.

Conversely, what's important here for Delaware-incorporated companies in this decision? What message do you hope boards take from this decision?

Seaman: The decision maintains the prerogative of boards to solicit information from stockholder nominees to ensure the electorate is sufficiently informed. But going forward, boards will have to carefully tailor information requests to solicit information that other stockholders may genuinely wish to know and to formulate the requests in clear language that can be understood and complied with. Boards must not, however, use disclosure requirements as traps to reject stockholder nominations and proposals and perpetuate the directors' tenure. The decision is a message to Delaware corporations that Delaware courts are paying attention to boards that design information requests to be invasive or burdensome or that effectively reserve the right to reject nomination notices through subjective or incomprehensibly worded prompts.

The Supreme Court's opinion closes: "We also note that, according to the Court of Chancery, Kellner submitted false and misleading responses to some of the requests. Given the court's countervailing findings about Kellner's and his nominees' deceptive conduct, no further action is warranted." So what's the practical impact here for your client?

Raile: The decision clears paths for our client to nominate a competing slate of directors for the board of this company, and he is currently weighing those options.

What will you remember most about handling this matter?

Goody Guillén: I'll remember clients and lawyers who collectively are passionate and determined to stand up to bullies and do what is right.

Seaman: I'll remember clients who had the courage and tenacity to take on a board of directors who manipulated AIM's bylaws in an attempt to preserve their board seats by ensuring that a contested corporate election would never occur.

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