

## ALERTS AND UPDATES

### Delaware Supreme Court Reverses Ruling on Term-Lengths for Directors Serving on Staggered Boards

December 15, 2010

The Delaware Supreme Court, in [Airgas, Inc. v. Air Products and Chemicals, Inc.](#),<sup>1</sup> reversed a Delaware Court of Chancery ruling that had upheld the validity of a bylaw amendment accelerating the annual meeting of the stockholders of Airgas from August to January, thereby allowing the stockholders to elect new directors to a class of the staggered board within a shorter time frame than usual.

#### Background

The Delaware Court of Chancery's decision arose from Air Products' hostile takeover bid to acquire Airgas and its proxy contest to gain control of the Airgas board.

At Airgas' 2010 annual meeting on September 15, 2010, Air Products, as part of its hostile takeover of Airgas, won all three board seats up for election on Airgas' nine-member staggered board. In addition, at this annual meeting, 51.8% of the shares present voted in favor of a bylaw amendment proposed by Air Products to move the annual stockholders' meeting – which historically had taken place during the month of August – up to January. This would result in Airgas' 2011 annual meeting being held barely four months after its 2010 annual meeting. It would also allow Air Products to present three additional director nominees and, if elected, would allow Air Products to win control of the Airgas board and subsequently to approve a merger with Air Products.

The key issue in the case was whether the bylaw amendment proposed by Air Products violated Airgas' governing documents and the Delaware General Corporation Law. The Court of Chancery concluded that the bylaw amendment was properly adopted at the September 15, 2010, annual meeting, that it did not conflict with Airgas' charter and that it was valid under Delaware law.

Airgas maintained that, in accordance with its bylaw which addresses director elections and their terms, the Air Products' bylaw amendment proposal required the approval of 67% of the shares entitled to vote at the annual meeting to pass, and that because it received only a simple majority vote, the bylaw was not adopted in accordance with Airgas' bylaws. Air Products contended that the supermajority requirement did not apply in this case. The Court of Chancery concluded that the bylaw amendment amended only the section of Airgas' bylaws addressing the annual stockholders' meeting, which required only a majority vote for stockholder approval and thus was validly adopted. The court further noted that "corporate charters and by-laws are contracts among the shareholders of a corporation and the general rules of contract interpretation are held to apply." Consequently, the court concluded, if the language of a contract is ambiguous, the court will look to the "common or ordinary meaning" of the language. Finally, the court observed that when presented with ambiguity in interpreting bylaws, "doubt is resolved in favor of the stockholders' electoral rights."

The main debate over the bylaw amendment's validity was a semantic one over the meanings of "annual" and "year," which were not clearly defined in either Airgas' organizational documents or under Delaware law. The specific language under consideration in Airgas' certificate of incorporation provided that at the annual meeting, "the successors to the class of Directors whose term expires at that meeting shall be elected to hold office for a term expiring at the annual meeting of stockholders held in the third year following the year of their election." The Court of Chancery, looking at the common dictionary definition of the word "annual" and interpreting the words in favor of the stockholder franchise, concluded that "annual" meant "occurring once a year"; and "annual meeting," read literally, means "a meeting that will take place once a year." The court noted that "corporations are free to draft their governing documents to specify when their annual meetings shall take place" and that Airgas had never specified in any of its corporate documents a minimum time period between meetings.

In deciding whether Delaware law was violated, the Court of Chancery held that Delaware law prescribes no minimum amount of time that must elapse between annual stockholders' meetings, but the only notable time restriction is that annual meetings cannot be separated by more than 13 months. There is no requirement, the court concluded, that the annual meeting must be spaced by 11 or 12 months, but just that it happens once a year, every year, and is spaced by no more than 13 months. The court held that since under Airgas' charter a director's "full term"

expires "in the third year" following the year of such director's election, the full terms of office shall expire at the annual meeting set in the third year after their election.

## **Delaware Supreme Court Opinion**

The Delaware Supreme Court reversed the decision of the Court of Chancery. Like the Court of Chancery, the Supreme Court found the language in Airgas' charter defining the duration of the directors' terms to be ambiguous. The Supreme Court thereupon determined to look to extrinsic evidence to interpret the intent of the charter language and concluded on that basis that the language "has been understood to mean that the Airgas directors serve three year terms." The extrinsic evidence examined by the Supreme Court included Delaware case law, charters and bylaws of Fortune 500 Delaware corporations with staggered boards, and model forms and commentary. The Supreme Court noted that Delaware courts had previously interpreted similar charter language to establish that directors of staggered boards served for three-year terms. Likewise, the Supreme Court noted that corporations with similar charter language "expressly represent in their proxy statements that their staggered-board directors serve three year terms."

Given the foregoing extrinsic evidence, the Supreme Court explained that, where extrinsic evidence resolves the ambiguity, effect must be given to the intended meaning of the parties as revealed by the circumstances surrounding its creation. Accordingly, the Supreme Court held that the bylaw was invalid because it "prematurely terminated" the three-year term of the directors provided by statute and Airgas' charter.

## **Conclusion**

This case serves as a reminder of the importance of precise and unambiguous language in a company's charter and bylaws. Notwithstanding the decision in this case, a company with a staggered board should, to avoid having ambiguous language in its organizational documents, consider specifying more precisely when the annual meeting takes place and the duration of the terms of members of the staggered board.

## **For Further Information**

If you have any questions regarding the issues or guidance described in this *Alert*, including how they may affect your company or its executives, please contact any [member](#) of the [Corporate Practice Group](#) or the attorney in the firm with whom you are mostly regularly in contact.

## **Note**

1. *Airgas, Inc. v. Air Prods. & Chems., Inc.*, 2010 Del. LEXIS 585 (Del. Nov. 23, 2010).

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