IN THE SUPREME COURT OF THE STATE OF DELAWARE

CA, Inc., a Delaware Corporation	§	**No. 329, 2008**
	§	
Petitioner Below	§	
Appellant	§	
	§	
	§	
	§	
v.	§	
	§	
AFSCME Employees Pension Plan	§	
	§	
Respondent Below	§	
Appellees.	§	

BRIEF OF APPELLEE

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Dated: July 7, 2008

TABLE OF CONTENTS

TABLE OF CITATIONS

Page(s)

CASES

STATUTES

OTHER AUTHORITIES

APPENDIX OF APPELLEE

I. NATURE OF PROCEEDINGS

This case is before the Court on two questions certified by the Securities and Exchange Commission (the "SEC") on June 27, 2008, and accepted by this Court on July 1, 2008, pursuant to Supreme Court Rule 31, as amended May 25, 2007.

II. SUMMARY OF ARGUMENT

1. The proposal (the "Proposal") submitted by the AFSCME Employees Pension Plan ("AFSCME") to CA, Inc. ("CA" or the "Company") deals with a fundamental aspect of the shareholder franchise – the process by which directors are nominated and elected. The Proposal advocates the adoption of a bylaw (the "Bylaw") which, if approved, would require the Company, under certain circumstances, to reimburse the reasonable expenses incurred by shareholders in connection with the solicitation of proxies in support of director candidates nominated by the shareholders *if* the candidates ultimately are elected to the board. The Bylaw is an appropriate subject for shareholder action precisely because it relates to the process of director elections. Delaware law historically has recognized that corporate boards do not have unfettered discretion to dictate the terms and processes for director elections. In fact Delaware courts have been reluctant to restrict shareholder action in this area absent clear and unambiguous language limiting shareholders' rights. CA argues that the Bylaw is not a proper subject matter for shareholder action because Section 141(a) of the DGCL vests

in the corporation's board the responsibility for managing the business and affairs of the corporation. Thus, CA submits, the shareholders' right to adopt bylaws under Section 109 cannot be read to limit the directors' managerial "discretion" under Section 141(a). Not only is CA's argument legally incorrect, it is wholly irrelevant for purposes of the present case. Even assuming *arguendo* that Section 141(a) could be read as creating a substantive limit on the ability of shareholders to adopt bylaws under Section 109, it is clear that Section 141(a) does *not* restrict shareholder action on matters relating to the election of directors. Accordingly, *even if* CA's overarching point has any merit, and it does not, the Court need not reach that issue to uphold the Bylaw in this case.

2. The Bylaw is an appropriate exercise of shareholder authority to adopt and amend corporate bylaws under Section 109 of the DGCL. Section 109(a) vests in shareholders the authority to adopt and amend corporate bylaws, and Section 109(b) does not draw distinctions regarding validity of bylaws based on the identity of who adopted them. Either the Bylaw is valid, or it is not valid. A valid bylaw is not rendered illegal simply if shareholders vote to adopt it. Indeed, so fundamental is the shareholders' right to adopt and amend bylaws that Section 109(a) precludes any attempt to limit that authority through corporate certificates or otherwise. It is equally clear that bylaws enacted by shareholders may greatly regulate the conduct of

corporate boards.[1] Thus, a bylaw that would require a corporation to reimburse proxy solicitation expenses, if legal under Delaware law (and it is), is not somehow rendered illegal simply because shareholders vote to adopt it. Given Delaware's historic policy of requiring a clear and unambiguous restriction on the shareholder franchise before limiting shareholders' statutory rights,[2] the Court should not interpret Section 141(a) to eliminate the ability of shareholders to adopt the Bylaw here.

3. Finally, CA also is wrong that the Bylaw somehow would cause CA to violate Delaware law. There is absolutely nothing in the DGCL or CA's certificate of incorporation that would render invalid a bylaw that would require the Company to reimburse proxy solicitation expenses incurred in connection with a successful campaign to elect directors to the Company's board. Delaware courts, including this Court, routinely have upheld bylaw provisions that require the expenditure of corporate funds.[3] Delaware law is also clear that corporations may reimburse the proxy expenses incurred by director candidates – whether incumbent or nominated by shareholders – upon election to the

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[1] *See, e.g., Frantz Mfg. Co. v. EAC Indus.*, 501 A.2d 401 (Del. 1985)

[2] *Id.*

[3] *See, e.g., Hibbert v. Hollywood Park, Inc.*, 457 A.2d 339, 343 (Del. 1983) (enforcing bylaw requiring indemnification).

board.[4] The mere fact that the Bylaw would require the expenditure of corporate funds, therefore, does not place the Bylaw in violation of Section 141(a). To the contrary, Section 141(a) merely charges corporate boards with the responsibility of managing the affairs of a corporation. CA's certificate of incorporation, which mirrors Section 141(a), does nothing more. But in exercising that managerial duty, the directors remain bound by the terms of the corporation's bylaws. Thus, there is nothing in Delaware law that would preclude the adoption of the Bylaw in this case.

[4] *Hall v. Trans-Lux Daylight Picture Screen Corp.*, 171 A. 226, 227 (Del. Ch. 1934)(allowing reimbursement of proxy expenses incurred by incumbent directors seeking reelection); *Steinberg v. Adams,* 90 F. Supp. 604, 607-08 (S.D.N.Y. 1950) (applying Delaware law, allowing reimbursement of expenses of successful insurgents incurred in a proxy contest).

III. STATEMENT OF FACTS

A. Factual Background

On March 13, 2008, AFSCME submitted a shareholder proposal (the "Proposal") to be included in CA's 2008 proxy statement, pursuant to 17 C.F.R. § 240.14a-8 ("Rule 14a-8"). Rule 14a-8 requires companies to place shareholder proposals that meet certain procedural and substantive requirements in their proxy statement. The Proposal advocates the adoption of a Bylaw that, if adopted, would require the Company, in certain circumstances, to reimburse reasonable proxy solicitation expenses incurred by shareholders (the "Nominator") who nominate director candidates *if* at least one of their sponsored candidates is elected to the Board. The proposed Bylaw reads as follows:

> RESOLVED, that pursuant to section 109 of the Delaware General Corporation Law and Article IX of the bylaws of CA, Inc., stockholders of CA hereby amend the bylaws to add the following Section 14 to Article II:
>
> The board of directors shall cause the corporation to reimburse a stockholder or group of stockholders (together, the "Nominator") for reasonable expenses ("Expenses") incurred in connection with nominating one or more candidates in a contested election of directors, including, without limitation, printing, mailing, legal, solicitation, travel, advertising and public relations expenses, so long as (a) the election of fewer than 50% of the directors to be elected is contested in the election, (b) one or more candidates nominated by the Nominator are elected to the corporation's board of directors, (c) stockholders are not permitted to cumulate their votes for directors, and (d) the election occurred, and the Expenses were incurred, after this bylaw's adoption. The amount paid to a Nominator under this bylaw in respect of a contested election shall not exceed the amount

expended by the corporation in connection with such election.

On April 18, 2008, CA sent a letter notifying the Staff of the SEC's Division of Corporation Finance (the "Division") of its intention to exclude the Proposal from its 2008 proxy materials, and requesting that the Staff concur with its belief that the Proposal is excludable under Rule 14a-8 (the "No-Action Request"). CA's letter argued that the Proposal was excludable under SEC Rule 14a-8(i)(1)-(3) and (8), 17 C.F.R. § 240.14a-8(i)(1)-(3),(8).[5] Attached to its No-Action Request, CA submitted a letter from its counsel Richards Layton & Finger, P.A., opining that the Proposed Bylaw would cause the Company to violated Delaware law if enacted and is not a proper action for shareholders under Delaware law (the "RLF Opinion").

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[5]

- Rule 14a-8(i)(1) allows companies to exclude proposals if they are not "not a proper subject for action by shareholders under the laws of the jurisdiction of the company's organization."
- Rule 14a-8(i)(2) allows companies to exclude proposals if they would "cause the company to violate any state, federal, or foreign law to which it is subject."
- Rule 14a-8(i)(3) allows companies to exclude proposals if they "If the proposal or supporting statement is contrary to any of the Commission's proxy rules."
- Rule 14a-8(i)(8) allows companies to exclude proposals if they "relate[] to a nomination or an election for membership on the company's board of directors or analogous governing body or a procedure for such nomination or election"

AFSCME responded to the No-Action Request on May 21, 2008, arguing that the Proposal could not be excluded under any of the provisions of SEC Rule 14a-8(i) identified by CA. With its response, AFSCME submitted an opinion letter from its counsel, Grant & Eisenhofer P.A., arguing that the Proposed Bylaw was entirely consistent with state law and a proper action for shareholders.

B. Procedural History

On June 27, 2008, the Division responded to CA's No-Action Request, stating that it was "unable to concur" with CA's opinion that the Proposal could be excluded under either SEC Rule 14a-8(i)(3) or Rule 14a-8(i)(8). However, pursuant to Section 11(8) of Article IV of the Delaware Constitution, which gives this Court jurisdiction to hear questions certified by the Commission, the Staff notified the parties that the Commission certified the following two questions to this Court: "(1) whether the proposal is a proper subject for action by shareholders as a matter of Delaware law, and (2) whether the proposal, if adopted, would cause CA to violate any Delaware law to which it is subject."[6]

On July 1, 2008, this Court issued an order stating that it would accept the questions certified to it by the Commission pursuant to Supreme Court Rule 31, as amended May 15, 2007, which

[6] *CA, Inc.*, SEC No-Action Letter, 2008 WL 2568454 (June 27, 2008).

allows the Court to accept certification where the questions of law deal with unsettled issues of state law.[7]

[7] *See* Order dated July 1, 2008.

IV. ARGUMENT

A. The Adoption Of A Bylaw Requiring Reimbursement For Director Candidates Nominated By Shareholders And Elected To The Board Is A Proper Subject For Action By CA's Shareholders.

1. Question Presented

Is the AFSCME Proposal a proper subject for action by shareholders as a matter of Delaware Law?

2. Scope of Review

Because this case concerns a certified question of law, the normal standards of review do not apply.[8] However, "[t]he scope of the issues that may be considered in addressing a certified question is limited by the procedural posture of the case."[9] To address the question certified by the SEC, this Court must determine whether AFSCME's Proposal, on its face, is a proper subject for action by shareholders.

3. Merits of Argument

a. AFSCME's Proposal Is A Proper Subject Matter For Shareholder Action Because It Concerns The Shareholders' Voting Franchise.

AFSCME's Proposal deals with an issue that is fundamental to the shareholder franchise – the election of directors. The Proposal recommends the adoption of a Bylaw that, if approved,

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[8] *Rales v. Blasband*, 634 A.2d 927, 931 (Del. 1993) ("Because we are addressing a certified question of law, as distinct from a review of a lower court decision, the normal standards of review do not apply.").

[9] *Id*.

would require the Company, under certain circumstances, to reimburse the proxy solicitation expenses incurred by shareholders who nominate director candidates if those candidates are successfully elected by shareholders for membership on the Company's Board of Directors. Precisely because the Bylaw concerns the process of the nomination and election of directors, it is an appropriate subject matter for shareholder action under established Delaware law. "Delaware courts have long exercised a most sensitive and protective regard for the free and effective exercise of voting rights."[10] Thus, in matters relating to director elections, Delaware courts not only have protected and encouraged the ability of shareholders to participate in the process, but have been highly critical of any attempt by directors to limit or make more difficult shareholder action in this area.[11] As this Court in *MM Companies, Inc. v. Liquid Audio, Inc.* held:

> Maintaining a proper balance in the allocation of power between the stockholders' right to elect directors and the board of directors' right to manage

[10] *Blasius Indus., Inc. v. Atlas Corp.*, 564 A.2d 651, 660 n.2 (Del. Ch. 1988).

[11] *See MM Cos., Inc. v. Liquid Audio, Inc.*, 813 A.2d 1118, 1128 (Del. Ch. 2003)("[The] deferential traditional business judgment rule standard is inappropriate when a board of directors acts for the *primary* purpose of impeding or interfering with the effectiveness of a shareholder vote."); *Unitrin, Inc. v. American General Corp.*, 651 A.2d 1361, 1378 (Del. 1995) ("This Court has been and remains assiduous in its concern about defensive actions designed to thwart the essence of corporate democracy by disenfranchising shareholders.").

> the corporation is dependent upon the stockholders' *unimpeded* right to vote effectively in an election of directors. This Court has repeatedly stated that, if the stockholders are not satisfied with the management or actions of their elected representatives on the board of directors, the power of corporate democracy is available to the stockholders to replace the incumbent directors when they stand for re-election.[12]

Delaware's historic protection of shareholders' ability to meaningfully participate in the election process stems from the recognition that "[t]he shareholder franchise is the ideological underpinning upon which the legitimacy of directorial power rests."[13] The integrity of the voting process, therefore, and the ability of shareholders to meaningfully participate in the process, "is critical to the theory that legitimates the exercise of power by some (directors and officers) over vast aggregations of property that they do not own."[14] It is for this reason that courts have recognized that the electoral process in corporations involves issues that are well beyond the statutory delegation of managerial responsibility to a company's board of directors: "[W]hen viewed from a broad, institutional perspective, it can be seen that matters involving the integrity of the shareholder

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[12] 813 A.2d at 1127 (emphasis added).

[13] *Centaur Partners, IV v. Nat'l Intergroup, Inc.*, 582 A.2d 923, 927 (Del. 1990), quoting *Blasius*, 564 A.2d at 659.

[14] *Blasius*, 564 A.2d at 659.

voting process involve considerations not present in any other context in which directors exercise delegated power."[15]

Under Delaware law, the shareholder franchise is *not* just limited solely to shareholders' ability to cast a vote at an annual meeting. Rather, "Delaware law recognizes that the 'right of shareholders to participate in the voting process includes the right to nominate an opposing slate.'"[16] In *Harrah's Entertainment, Inc. v. JCC Holding Co.*, for example, the court recognized that "[t]he unadorned right to cast a ballot in a contest for [corporate] office is meaningless without the right to participate in selecting the contestants. As the nominating process circumscribes the range of choice to be made, it is a fundamental and outcome-determinative step in the election of officeholders."[17] Because the nomination process is an integral element of the shareholder franchise, the Proposed Bylaw

[15] *Blasius*, 564 A.2d at 659-60 ("[I]t appears that the ordinary considerations to which the business judgment rule originally responded are simply not present in the shareholder voting context. That is, a decision by the board to act for the primary purpose of preventing the effectiveness of a shareholder vote inevitably involves the question who, as between the principal and the agent, has authority with respect to a matter of internal corporate governance. That, of course, is true in a very specific way in this case which deals with the question who should constitute the board of directors of the corporation, but it will be true in every instance in which an incumbent board seeks to thwart a shareholder majority.")

[16] *Harrah's Entertainment, Inc. v. JCC Holding Co.*, 802 A.2d 294, 310 (Del. Ch. 2002).

[17] *Harrah's Entertainment*, 802 A.2d at 311, quoting *Durkin v. Nat'l Bank of Olyphant*, 772 F.2d 55, 59 (3d Cir. 1985)

addresses an area that is an appropriate subject matter for shareholder action.

That the process governing the nomination and election of corporate directors is an appropriate subject matter for shareholder action is, or at least should be, a rather unremarkable proposition. Indeed, because the integrity of the shareholder vote "legitimize[s] the exercise of power"[18] by corporate boards, ceding complete discretion to directors to set the rules governing election process would de-legitimize the very source of their power. It is precisely for this reason that, rather than permitting directors an unfettered right to dictate the terms for corporate elections, there exists in Delaware "a general policy against disenfranchisement"[19] that requires any restriction on shareholders' rights to be set forth in "clear and unambiguous" terms.[20]

b. The Proposed Bylaw Is Authorized Under Section 109(b) Of The DGCL

"The power to make and amend the bylaws of a corporation has long been recognized as an inherent feature of the corporate structure."[21] The bylaws of a corporation are "the self-imposed rules and regulations deemed expedient for [the] convenient

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[18] *Blasius*, 564 A.2d at 659.

[19] *Centaur Partners*, 582 A.2d at 927.

[20] *Id.*

[21] *Frantz Mfg. Co. v. EAC Indus.*, 501 A.2d 401, 407 (Del. 1985)

functioning" of the corporation.[22] Consistent with the DGCL's overall design to provide corporations with maximum flexibility in structuring their internal operations,[23] Section 109(b), which contains the only limitation on the subject matter of bylaws, defines the scope of permissible bylaws very broadly:

> (b) The bylaws may contain any provision, not inconsistent with law or with the certificate of incorporation, relating the business of the corporation, the conduct of its affairs, and its rights or powers or the rights or powers of its stockholders, directors, officers or employees.[24]

The relevant question for purposes of this case is whether the Bylaw is "inconsistent with law" or violates any provision in

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[22] *Gow v. Consolidated Coppermines Corp.*, 165 A. 136, 140 (Del. Ch. 1933); *see also Hollinger Intern. v. Black*, 844 A.2d 1022, 1078 (Del. Ch. 2005), *aff'd*, 872 A.2d 559 (Del. 2005) ("Traditionally, the bylaws have been the corporate instrument used to set forth the rules by which the corporate board conducts its business.").

[23] *See*, *e.g.*, *Hollinger Intrn.*, 844 A.2d at 1078 ("The DGCL is intentionally designed to provide directors and stockholders with flexible authority, permitting great discretion for private ordering and adaptation."); *Jones Apparel Group, Inc. v. Maxwell Shoe Co., Inc.*, 883 A.2d 837, 845 (Del. Ch. 2004) ("Delaware's corporate statute is widely regarded as the most flexible in the nation because it leaves the parties to the corporate contract (managers and stockholders) with great leeway to structure their relations, subject to relatively loose statutory constraints and to the policing of director misconduct through equitable review. As Professor Folk noted in his comments on the 1969 amendments to the DGCL, and particularly on the enabling feature of § 141(a), 'the Delaware corporation enjoys the broadest grant of power in the English-speaking world to establish the most appropriate internal organization and structure for the enterprise.'")(quoting Ernest L. Folk, III, Amendments to the Delaware General Corporation Law 5 (1969)).

[24] 8 Del. C. § 109(b).

CA's certificate of incorporation. In this regard, however, it is important to note that "[t]he bylaws of a corporation are presumed to be valid, and the courts will construe the bylaws in a manner consistent with the law rather than strike down the bylaws."[25]

This Court has observed: "The Delaware General Corporation Law affords considerable flexibility in the construction of mechanisms for corporate governance and control."[26] As explained below, AFSCME's Proposed Bylaw would represent a proper exercise of shareholders' statutory rights under Section 109 of the DGCL, does not unlawfully restrict the director's managerial responsibility under Section 141(a) of the DGCL, and nothing in the DGCL or CA's certificate of incorporation clearly and unambiguously bars shareholders from deciding to adopt a bylaw designed to facilitate and encourage meaningful director elections.

c. The Managerial Responsibility Vested In Corporate Boards Under Section 141(a) Does Not Preclude Shareholders From Adopting A Bylaw Relating To The Election Process.

Before the SEC, CA argued that the Bylaw did not present a proper subject matter for shareholder action under Delaware law because Section 141(a) of the DGCL vests in corporate boards the "power" to manage the business and affairs of the corporation,

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[25] *Frantz Mfg.*, 501 A.2d at 407.

[26] *Centaur Partners*, 582 A.2d at 927.

and that shareholders' ability to amend bylaws under Section 109(a) should not be interpreted in such a manner as to "require that the Board relinquish its power" that supposedly is vested under Section 141(a)[27] CA's argument is misplaced. Delaware courts have *never* interpreted this statutory delegation as giving corporate boards unfettered discretion in matters relating to the process of the nomination and election of directors. Rather, "Delaware courts have long exercised a most sensitive and protective regard for the free and effective exercise of voting rights."[28] Thus, in matters relating to director elections, Delaware courts not only have protected and encouraged the ability of shareholders to participate in the process, but have been highly critical of any attempt by directors to limit or make more difficult shareholder action in this area.[29]

As an initial matter, whether, and to what extent, the statutory delegation of managerial responsibility to corporate

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[27] RLF Opinion at 4.

[28] *Blasius Indus.*, 564 A.2d at 660 n.2; *see also Aronson v. Lewis*, 473 A.2d 805, 811 (Del. 1984), *overruled on other grounds, Brehm v. Eisner*, 746 A.2d 244 (Del. 2000)(holding that shareholders may use the "machinery of corporate democracy" to address dissatisfaction with directors).

[29] *See MM Cos.*, 813 A.2d at 1128 ("[The] deferential traditional business judgment rule standard is inappropriate when a board of directors acts for the *primary* purpose of impeding or interfering with the effectiveness of a shareholder vote."); *Unitrin, Inc. v. American General Corp.*, 651 A.2d 1361, 1378 (Del. 1995) ("This Court has been and remains assiduous in its concern about defensive actions designed to thwart the essence of corporate democracy by disenfranchising shareholders.").

directors under Section 141(a) limits or restricts shareholders' ability to amend bylaws under Section 109, presents an issue that the Court need not address at this time. *Even if* Section 141(a) can, in some respect, restrict what kinds of bylaws shareholders can adopt under Section 109, it is clear that Section 141(a) does not, and was not intended to, limit shareholders' ability to act on matters relating to the process of electing directors. Accordingly, even if CA is theoretically correct regarding the interplay between Sections 109 and 141(a), CA's point is irrelevant here. Section 141(a) *cannot* be read to prevent shareholders from adopting a bylaw establishing a process relating to the election of directors. The statutory delegation of managerial responsibility to corporate directors under Section 141(a) does not "clear[ly] and unambiguous[ly]" restrict the ability of CA's shareholders to consider and adopt the Proposed Bylaw advanced by AFSCME here and, given Delaware's policy against disenfranchisement, the Bylaw is an appropriate subject matter for shareholder action.

Under Section 141(a) of the DGCL, the responsibility for the management of the business and affairs of the corporation is delegated to the board of directors.[30] Pursuant to this provision, Delaware courts have recognized that Section 141(a) "imposes on a board of directors the duty to manage the business

[30] 8 Del. C. § 141(a).

and affairs of the corporation."[31] This managerial responsibility, however, is subject to the bylaws, which may regulate how directors exercise their duties to shareholders. Indeed, Section 109(b) of the DGCL unambiguously states that bylaws may regulate the "rights or powers of [the corporation's] ... directors ..."[32]

Shareholders' ability to enact bylaws that regulate the Board of directors has been affirmed numerous times in Delaware courts. In *Frantz Mfg. Co. v. EAC Industries*,[33] this Court upheld the validity of a shareholder-enacted bylaw that "required attendance of all directors for a quorum and unanimous approval of the board of directors before board action [could] be taken, and they thereby limited the functioning of the Frantz board."[34]

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[31] *Paramount Communications, Inc. v. Time Inc.*, 571 A.2d 1140, 1150 (Del. 1989). The obligation of directors to manage the business and affairs of a corporation provided in Section 141(a) is a duty and a privilege. It is a *responsibility* to exercise one's fiduciary duties, and not a vested right to exercise unfettered discretion in the management of a corporation. *See Stellini v. Oratorio*, 1979 WL 2703, *2 (Del. Ch.) ("Clearly, as directors, the plaintiffs had no vested interest in a directorship of [corporation]. Rather, any right which they may have held in the office of director was acquired with the actual or implied knowledge that such right could be extinguished by the vote or consent of the majority stockholders of the defendant corporation.").

[32] 8 Del. C. § 109(b)

[33] 501 A.2d 401 (Del. 1985)

[34] 501 A.2d at 407.

Similarly, in *American Int'l Rent a Car, Inc v. Cross*,[35] the Court of Chancery, in rejecting a shareholder challenge to a board-enacted bylaw amendment, held:

> If a majority of American International's stockholders in fact disapproved of a Board's amendment of the bylaw, several recourses were, and continue to be, available to them. They could vote the incumbent directors out of office. *Alternatively, they could cause a special meeting of the stockholders to be held for the purpose of amending the bylaws and, as part of the amendment, they could remove from the Board the power to further amend the provision in question*.[36]

More recently, in *Hollinger Int'l, Inc. v. Black,*[37] Vice Chancellor Strine relied upon this Court's decision in *Frantz* in holding that "[b]ylaws [can] impose severe requirements on the conduct of a board without running afoul of the DGCL."[38] Because "bylaws are generally thought of as having a hierarchical status greater than board resolutions, ... a board cannot override a bylaw requirement by merely adopting a resolution."[39] Thus, in that case, the Court held that a bylaw that dissolved a committee

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[35] 1984 WL 8204 (Del. Ch.).

[36] *Id.* at *3; *see also Hollinger*, 844 A.2d at 1078-9 ("By its plain terms, § 109 provides stockholders with a broad right to adopt bylaws 'relating to the business of the corporation, the conduct of its affairs, and its rights or powers or the rights or powers of its stockholders, directors, officers or employees.")(internal citation omitted).

[37] 844 A.2d 1022 (Del. Ch. 2004), *aff'd* 872 A.2d 559 (Del. 2005)

[38] *Id.* at 1079.

[39] *Id*. at 1080.

established by the Board did not violate Section 141(a) merely because it interfered with the board's managerial discretion:

> For similar reasons, I reject International's argument that that provision in the Bylaw Amendments impermissibly interferes with the board's authority under § 141(a) to manage the business and affairs of the corporation. *Sections 109 and 141, taken in totality, and read in light of Frantz, make clear that bylaws may pervasively and strictly regulate the process by which boards act, subject to the constraints of equity.*[40]

Thus, merely because the proposed Bylaw would regulate director conduct does not make the Bylaw impermissible under Delaware law.

Nevertheless, CA argues that shareholders may only enact bylaws if a specific provision of the DGCL authorizes a bylaw on a particular subject; in the absence of such specific statutory authorization, the argument goes, *any* bylaw adopted by shareholders would violate Section 141(a).[41] There are two major problems with CA's argument in this regard. First, CA's argument, if adopted, would render a portion of Section 109 completely irrelevant. Second, CA's argument that directors necessarily have rights to amend bylaws that are somehow superior to those of shareholders is fundamentally inconsistent with the structure of the statute.

CA's argument violates fundamental principles of statutory construction because, if accepted, it would render Section 109(b)

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[40] *Id*. at 1080 n. 136 (emphasis added).

[41] RLF Opinion at 3 n.1.

entirely superfluous. To explain, if shareholders were limited to enacting bylaws only involving subject areas where other provisions of the DGCL specifically permitted the adoption of bylaws, the provision in Section 109(b) that the bylaws may contain "any provision" that is "not inconsistent with law" would be wholly irrelevant. The legislature simply could have included Section 109(a) authorizing the adoption of bylaws, and ended the statute there. But they did not. By specifically permitting the adoption of bylaws on any matter "not inconsistent with law" (as distinguished from "specifically authorized by law"), the legislature exhibited a plain intent to permit shareholders (and directors, if permitted by the certificate) to adopt bylaws on areas that are *not* specifically addressed in other sections of the DGCL. CA's argument, which would render the expansive provisions of Section 109(b) a nullity, simply cannot be credited. This Court has observed that "In determining legislative intent in this case, we find it important to give effect to the whole statute, and leave no part superfluous."[42]

Indeed, CA's argument has been specifically rejected by Chancellor Chandler in *Unisuper Ltd. v. News Corp.*[43]. In that case, the Chancellor constructed Section 141(a) in way that would

[42] *Keeler v. Harford Mut. Ins. Co.*, 672 A.2d 1012, 1016 (Del. 1996).

[43] 2005 WL 3529317 (Del. Ch.), *appeal refused by*, 906 A.2d 138 (Del. 2006).

not render Section 109(b) superfluous and is wholly consistent with Delaware case law establishing that shareholders may regulate director conduct through bylaws.[44] Specifically, the Chancery Court in *News Corp*. held that while Section 141(a) restricts directors from abdicating their fiduciary duty to third parties, it does not prohibit shareholders, the true owners of the Company, from regulating the conduct of directors.[45]

In that case, the defendants argued that a contract with shareholders was invalid because the board agreed not to enact a poison pill for successive one year terms without shareholder approval. The defendants argued that the contract was "inconsistent with the general grant of managerial authority to the board in Section 141(a)."[46] The court disagreed, holding that allowing shareholders to vote on corporate matters was not a delegation of managerial authority inconsistent with Section 141(a):

> Delaware's corporation law vests managerial power in the board of directors because it is not feasible for shareholders, the owners of the corporation, to exercise day-to-day power over the company's business and affairs. Nonetheless, when shareholders exercise their right to vote in order to assert control over the business and affairs of the corporation the board must give way. *This is because the board's power-which is that of an agent's with regard to its principal -*

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[44] *Id.* at *6.

[45] *Id.* at *6-8.

[46] *Id*. at *6.

> *derives from the shareholders, who are the ultimate holders of power under Delaware law*.[47]

Because of this relationship, akin to that between an agent and principal, directors cannot use the grant of managerial power in Section 141(a) as an impediment to shareholder action. The court in *News Corp*. held:

> Fiduciary duties exist in order to fill the gaps in the contractual relationship between shareholders and directors of the corporation. *Fiduciary duties cannot be used to silence shareholders and prevent them from specifying what the corporate contract is to say. Shareholders should be permitted to fill a particular gap in the corporate contract if they wish to fill it.* This point can be made by reference to principles of agency law: Agents frequently have to act in situations where they do not know exactly how their principal would like them to act. In such situations, the law says the agent must act in the best interest of the principal. *Where the principal wishes to make known to the agent exactly which actions the principal wishes to be taken, the agent cannot refuse to listen on the grounds that this is not in the best interest of the principal.*[48]

Additionally, the court in *News Corp*. held that a shareholder-enacted bylaw was an appropriate means for shareholders to exert control over the company. The court held: "Of course, the board of directors' managerial power is not unlimited ... [T]he Delaware General Corporations Law vests shareholders with the power to adopt, amend or repeal bylaws

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[47] *Id*. at *6 (emphasis added).

[48] *Id*. at *8.

relating to the business of the corporation and the conduct of its affairs."[49]

CA's argument is also fundamentally at odds with the statutory scheme of Section 109 and the DGCL in general. Specifically, under Section 109(a), the right to adopt and amend bylaws is vested, unequivocally, in the shareholders, and directors may adopt bylaws *only if* the power is so vested to them in a specific provision in the certificate of incorporation.[50] But even if the certificate grants directors such authority, such provision "shall not divest the stockholders ... of the power, nor limit their power to adopt, amend or repeal bylaws."[51] Thus, at most, the right of directors to adopt and amend bylaws can only be ***coextensive with and not superior to*** the right of the shareholders to do the same, and is conditioned on an express grant of such authority in the company's certificate of incorporation. It would be wholly inconsistent with the statutory structure of Section 109(a) to hold that, although shareholders have a statutory right to adopt and amend bylaws, and directors can only exercise such right if it is expressly granted to them in a company's certificate, directors can adopt bylaws that the shareholders themselves are precluded from

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[49] *Id.* at *6 (emphasis added).

[50] 8 Del. C. § 109(a).

[51] 8 Del. C. § 109(a).

adopting. The simple point is either the bylaw is valid, or it is not. Either the bylaw is a proper exercise of authority under Section 109, or it is not. A bylaw that is permissible under Section 109 is not somehow rendered illegal simply because shareholders vote to adopt it.

It is important to note that Delaware courts have *never* struck down a shareholder-enacted bylaw because it was inconsistent with Section 141(a). As a result, the RLF Opinion attempted to analyze case law where ***director conduct*** was held to violate Section 141(a). However, cases addressing situations where *directors* improperly abdicate their fiduciary duties have nothing to do with whether *shareholders* may enact bylaws that regulate the conduct of the corporations they own. In *Quickturn Design Sys. v. Shapiro*,[52] this Court held that directors could not amend a poison pill in a manner that disabled future directors' ability to redeem it for six months. The Court held that the poison pill amendment would impermissibly "prevent[] a newly elected board of directors from completely discharging its fiduciary duties."[53] Thus, the board would cause future directors to abdicate their fiduciary duty. Similarly, in *Abercrombie v. Davies*,[54] the court invalidated an agreement between a number of

[52] 721 A.2d 1281, 1289-90 (Del. 1998) (cited by RLF Opinion at 6).

[53] *Id*. at 1292.

[54] 123 A.2d 893, 897 (Del. Ch. 1956) (cited by RLF Opinion at 6)

directors and a number of stockholders of a corporation in which the directors who were party to the contract agreed to always vote similarly on issues. In that case, the court held that directors had contracted to vote in a specified manner even though such vote may be "contrary to their own best judgment."[55]

Before the SEC, CA cited cases for the unremarkable proposition that generally Section 141(a) of the DGCL vests power in directors to manage the affairs of the corporation. The cases cited by CA, however, simply do not address the issue presented here: whether shareholders, acting collectively, may enact a bylaw regulating how directors fulfill their duty.[56] They are simply not contrary to *Frantz*, *News Corp.*, and *Hollinger*, which hold that shareholders have broad power to enact bylaws that set restrictions on how directors can exercise discretion in fulfilling their managerial responsibilities.[57]

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[55] *Id*. at 899.

[56] *See* RLF Opinion at 6-7 (quoting *Aronson v. Lewis*, 473 A.2d 805, 811 (Del. 1984) (holding that shareholder bringing derivative suit did not allege that demand was excused); *McMullin v. Beran*, 765 A.2d 910, 916 (Del. 2000) (holding plaintiff adequately pled that the directors breached their fiduciary duties to minority shareholders in selling the company to a third party); *Maldonado v. Flynn*, 413 A.2d 1251, 1255 (Del. Ch. 1980), *rev'd on other grounds sub nom.*, *Zapata Corp. v. Maldonado*, 430 A.2d 779 (Del. 1981) (holding that board could not compel dismissal of a derivative lawsuit brought by a shareholder after it refused demand); *Norte & Co. v. Manor Healthcare Corp.*, 1985 WL 44684, at *5 (Del. Ch. 1985) (holding "convertible debenture holders may not state a claim for breach of fiduciary duty").

[57] CA's reliance on *Paramount Commc'ns, Inc. v. Time Inc.*, 1989 WL 79880, at *30 (Del. Ch. 1989), *aff'd*, 571 A.2d 1140 (Del.

B. A Bylaw Requiring The Reimbursement Of Proxy Solicitation Expenses Would Not Cause CA To Violate Delaware Law Or The Company's Certificate Of Incorporation.

1. Question Presented

Would the AFSCME Proposal, if adopted, cause CA to violate any Delaware law to which it is subject?

2. Scope of Review

Because this case concerns a certified question of law, the normal standards of review do not apply.[58] However, "[t]he scope of the issues that may be considered in addressing a certified question is limited by the procedural posture of the case."[59] To address the question certified by the SEC, this Court must determine whether the Proposed Bylaw, on its face, would cause the company to violate Delaware law if enacted.

3. Merits of Argument

The proposed Bylaw is intended to improve corporate governance at CA by encouraging shareholders to expend reasonable funds to help elect directors who shareholders feel are qualified to be directors, by giving them a reasonable expectation of being

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1980), is also misplaced. In that case, the Court held that a board may maintain a poison pill, even if a majority of shareholders wished to tender their shares. This has nothing to do with whether bylaws can regulate the process by which a corporation's directors expend corporate funds.

[58] *Rales v. Blasband*, 634 A.2d at 931 ("Because we are addressing a certified question of law, as distinct from a review of a lower court decision, the normal standards of review do not apply.").

[59] *Id*.

reimbursed if their candidates are elected. It is entirely permissible for a company to reimburse funds expended to elect a slate of directors nominated by shareholders, and it is entirely permissible under Delaware law for bylaws to provide for mandatory reimbursement. Adoption of the Bylaw, therefore, would not cause CA to violate any provision of Delaware law.

a. Corporate Bylaws Can Require Mandatory Payments Out Of The Corporate Treasury Without Violating Section 141(a).

In addition to regulating board conduct, bylaws appropriately can require mandatory payments out of the Company's treasury. Under Delaware law, corporate charters and bylaws generally are regarded and enforced as contracts between the shareholders the directors.[60] Thus, if the bylaws make a certain payment mandatory, Delaware will enforce the provision in accordance with its contractual terms.

For example, Delaware courts routinely uphold and enforce bylaws requiring mandatory indemnification of directors in connection with lawsuits relating to their positions on the board.[61] Although it is true that the DGCL specifically permits

[60] *See generally Centaur Partners,* 582 A.2d at 928 ("Corporate charters and by-laws are contracts among the shareholders ...").

[61] *See Orloff v. Shulman*, 2005 WL 5750635 (Del. Ch.)(enforcing mandatory indemnification bylaw adopted by directors in anticipation of immediate threat of litigation); *Underbrink v. Warrior Energy Services Corp*., 2008 WL 2262316 (Del. Ch.) (enforcing mandatory retroactive indemnification bylaw adopted by directors adopted under imminent threat of litigation).

corporations to make such payments under certain circumstances,[62] the relevant statute is entirely silent on the issue of bylaws, and does not make reimbursement mandatory.[63] Nevertheless, Delaware courts consistently have held that "a corporation can make the right to advancement of expenses mandatory, through a provision in its certificate of incorporation *or bylaws*."[64] While in the absence of such a provision, the decision to indemnify a director generally is considered within and subject to the

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[62] For example, Section 145(e) states:

> Expenses (including attorneys' fees) incurred by an officer or director in defending any civil, criminal, administrative or investigative action, suit or proceeding may be paid by the corporation in advance of the final disposition of such action, suit or proceeding upon receipt of an undertaking by or on behalf of such director or officer to repay such amount if it shall ultimately be determined that such person is not entitled to be indemnified by the corporation as authorized in this section. Such expenses (including attorneys' fees) incurred by former directors and officers or other employees and agents may be so paid upon such terms and conditions, if any, as the corporation deems appropriate.

8 Del. C. § 145(e). Similarly, Section 145(a) states: "A corporation shall have power to indemnify any person who was or is a party or is threatened to be made a party to any threatened, pending or completed action ..." 8 Del. C. § 145(a).

[63] *VonFeldt v. Stifel Financial Corp.* 714 A.2d 79, 81 (Del. 1998)("Section 145(a) authorizes, but does not require, indemnification in connection with third-party actions.").

[64] *Gentile v. SinglePoint Financial, Inc.*, 787 A.2d 102, 106 (Del.Ch. 2001)(emphasis added).

business judgment of the board,[65] a bylaw making indemnification mandatory removes any discretion from corporate boards to approve, or disapprove, such payments. As this Court has explained: "Section 145(a) authorizes, but does not require, indemnification in connection with third-party actions. Virtually all public corporations have extended indemnification guarantees ***via bylaw*** to cases where indemnification is typically only permissive."[66] In other words, "[w]here such a mandatory provision exists, the rights of potential recipients of such advancements will be enforced as a contract."[67]

Bylaws requiring the expenditure of corporate funds are not limited to provisions making mandatory the indemnification authorized under Section 145 of the DGCL. Indeed, Delaware corporations have bylaws requiring the companies to expend corporate funds on such items as salaries,[68] insurance,[69] travel

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[65] *Havens v. Attar*, 1997 WL 55957, *13 (Del. Ch.) ("a board's decision to accept an undertaking and to advance expenses is left to *the business judgment of the board in the absence of a by-law specifically providing for mandatory advancement*." (emphasis in original)).

[66] *VonFeldt*, 714 A.2d at 81 (internal quotations omitted) (emphasis added).

[67] *See Gentile*, 787 A.2d at 106 ("[A] a corporation can make the right to advancement of expenses mandatory, through a provision in its certificate of incorporation or bylaws ... Where such a mandatory provision exists, the rights of potential recipients of such advancements will be enforced as a contract.").

[68] *See* Coca Cola Co., Bylaws, Art. II, Sec. 9 (B-40).

[69] *See* ABM Industries Inc., Bylaws, Art. VII, Sec. 7.8 (B-72).

expenses,[70] and office space in particular locations.[71] The simple point is that bylaws can require the mandatory payment of corporate funds without improperly interfering with the directors' responsibility to manage the business and affairs of a corporation under Section 141(a).[72]

b. Because Corporations May Reimburse Proxy Expenses Incurred By Successfully Elected Directors Nominated By Shareholders, A Bylaw Making Such Reimbursement Mandatory Is Permissible.

It is well established that corporations may reimburse directors for expenses incurred in connection with a proxy solicitation. Almost 75 years ago, in *Hall v. Trans-Lux Daylight*

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[70] *See* Barnes & Noble Inc., Bylaws, Art. III, Sec. 10 (B-9); Citigroup, Inc., Bylaws, Art. IV, Sec. 3 (B-27).

[71] *See* Southern Co., Bylaws, Sec. 1 (B-45).

[72] Similarly, CA's citations to cases holding that directors have authority to expend corporate funds are inapposite because these cases simply do not discuss the issue of how shareholder-enacted bylaws may regulate director conduct. *See* RLF Opinion at 8 (quoting *Wilderman v. Wilderman*, 315 A.2d 610 (Del. Ch. 1974) (holding that unless board authorized compensation to an officer, the officer had to argue that such payment was allowable under "the theory of quantum meruit" to retain such payment); *Lewis v. Hirch*, 1994 WL 263551, at *3 (Del. Ch.) (approving settlement concerning excessive compensation over objection) ("Excessive compensation claims are difficult to prove at trial, largely because executive compensation is a matter ordinarily left to the business judgment of a company's board of directors."); *Alessi v. Beracha*, 849 A.2d 939, 943 (Del. Ch. 2004) (holding that it was a reasonable inference that directors knew about a company stock buy back program because DGCL § 141(a) created a duty for directors to manage the affairs of the corporation); *UIS, Inc. v. Walbro Corp.*, 1987 WL 18108, at *2 (Del. Ch.) (holding that the court would not freeze proceeds from issuance of preferred stock pending litigation because *the court* would not interfere with the directors' ability to control company funds).

Picture Screen Corp.,[73] for example, the Chancery Court held that incumbent directors were entitled to use corporate funds to pay for solicitation expenses incurred in connection with a contested election.[74] While most often incumbent directors are able to tap the company's coffers to fund a proxy contest, Delaware law also permits the reimbursement of expenses incurred on behalf of candidates nominated by shareholders and elected to the board.[75] As a federal court in New York court observed, applying Delaware law, "I see no reason why the stockholders should not be free to reimburse those whose expenditures succeeded in ridding a corporation of a policy frowned upon by a majority of the stockholders."[76]

Because the reimbursement of proxy expenses, for both incumbent directors and candidates nominated by shareholders who are elected to the board, is a permissive use of corporate funds, it is perfectly consistent with Delaware law to make such reimbursement mandatory through the adoption of a bylaw. As

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[73] 171 A. 226 (Del. Ch. 1934)

[74] *Id*. at 227

[75] *See Jana Master Fund, Ltd. v. CNET Networks, Inc.,* 2008 WL 660556, at*4 (Del.Ch.) ("Generally, although management is reimbursed for its proxy expenses from the corporate coffers, insurgent shareholders finance their own bid and can hope for reimbursement only if that bid is successful.").

[76] *Steinberg v. Adams,* 90 F. Supp. 604, 607-08 (S.D.N.Y. 1950) (applying Delaware law, allowing reimbursement of expenses of successful insurgents incurred in a proxy contest).

explained above, Delaware law authorizes, but does not require, companies to indemnify directors for expenses relating to litigation.[77] Delaware corporations can, however, make indemnification mandatory by including such a provision in the company's bylaws.[78] Similarly, because corporations are free to reimburse the proxy expenses of directors elected to corporate boards, there is no logical reason to preclude a company from making such reimbursement mandatory through a similar bylaw provision.

Before the SEC, CA argued that a bylaw making reimbursement mandatory would be improper because it would prevent the Company's directors from exercising discretion "to determine what expenses should and should not be reimbursed to stockholders."[79] Specifically, CA reasons that because Delaware caselaw establishes directors cannot, consistent with their fiduciary duties, authorize the reimbursement of proxy expenses incurred for no reasons other than to entrench a director in office, a bylaw making reimbursement mandatory somehow would be improper.[80]

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[77] 8 Del. C. § 145(a).

[78] *See Homestore, Inc. v. Tafeen*, 888 A.2d 204, 212 (Del. 2005) ("[M]andatory advancement provisions are set forth in a great many corporate charters, bylaws and indemnification agreements.").

[79] RLF Opinion at 4.

[80] RLF Opinion at 4 (citing *Hibbert v. Hollywood Park Inc.*, 457 A.2d 339, 345 (Del. 1983); *Hall v. Trans-Lux Daylight Picture Screen Corp.*, 171 A. 226, 227 (Del. Ch. 1934)).

CA's concerns are misplaced for two reasons. First, if reimbursement is mandatory under the terms of a bylaw, the directors would not be called upon to exercise any business judgment in authorizing reimbursement called for under the bylaw. Second, where Delaware courts have raised concerns regarding directors' decisions to indemnify or reimburse proxy solicitation expenses, they have done so based on a concern that the directors' decision to authorize reimbursement or indemnification in the particular case was the product of an improper entrenchment motive or self-dealing that placed personal interests above the interests of the corporation. These concerns simply are not implicated where a corporate board would be required to reimburse proxy solicitation expenses incurred in connection with the election of a director nominated by shareholders and not incumbent management.

If reimbursement remains discretionary, the CA directors would, of course, be constrained by their fiduciary obligations to the Company and its shareholders in evaluating whether to authorize the reimbursement of proxy solicitation expenses in any given case.[81] But if reimbursement is made mandatory through an

[81] In *Heinman v. Datapoint Corp.*, 611 A.2d 950, 953 (Del 1992), *overruled on other grounds by*, *Brehm v. Eisner*, 746 A.2d 244 (Del. 2000), for example, this Court held that a decision by insurgent directors elected to the board to cause a company to expend corporate funds to reimburse solicitation expenses was an interested transaction that implicated the directors' fiduciary duties and was subject to enhanced scrutiny: "The complaint alleges a successful contest for corporate control, with the

amendment to the Company's bylaws, the directors' would not be called upon to exercise their business judgment at all.

This was precisely the distinction recognized by the Court in *Underbrink v. Warrior Energy Services Corporation.*[82] In *Underbrink*, the plaintiff alleged that a corporation's directors breached their fiduciary duties by adopting a bylaw providing for the mandatory and retroactive reimbursement of litigation expenses at a time when the directors faced the imminent threat of litigation.[83] Specifically, the plaintiff alleged that in adopting the bylaw, the directors failed to conduct any analysis regarding the value of the specific reimbursement obligation or whether such reimbursement would be in the best interests of the company.[84] The Chancery Court rejected this analysis. Relying on the Chancery Court's previous decision in *Orloff v. Shulman*,[85] the Court reasoned that the decision to *adopt* a reimbursement bylaw did not implicate the same considerations that would be raised if

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victors in that contest using their newly acquired positions to cause the corporation to reimburse the costs of waging that contest. Proof of these facts at trial would represent a *prima facia* case of director self-dealing. *Weinberger v. UOP, Inc.*, Del.Supr., 457 A.2d 701, 710 (1983) ('When directors of a Delaware corporation are on both sides of a transaction, they are required to demonstrate their utmost good faith and the most scrupulous inherent fairness of the bargain.')."

[82] 2008 WL 2262316 (Del. Ch.)

[83] *Id*. at *1.

[84] *Id*. at *8-12.

[85] 2005 WL 5750635 (Del. Ch.)

the directors elected to *pay* reimbursement *in the absence* of such a mandatory requirement.[86] The Court observed:

> In *Orloff v. Shulman*, the plaintiffs alleged "the defendants approved [a mandatory advancement bylaw and a § 102(b)(7) charter provision] under the threat of imminent litigation, and breached their fiduciary duties by self-interestedly protecting themselves against litigation that they knew would soon name them as defendants ." With respect to the mandatory advancement bylaw, the court held the plaintiffs pled "no facts which suggest that the bylaw amendment at issue is unreasonable in this case. Therefore, it is not subject to further scrutiny by this court." Citing *Havens v. Attar*, the court limited its holding, however, to situations in which "plaintiffs challenge the adoption of a bylaw that requires the corporation to advance litigation costs sometime in the future rather than challenging the directors' decision to advance particular litigation expenses."
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> In *Havens*, the plaintiffs argued the defendant directors breached their duties of care and loyalty in advancing litigation expenses in the absence of a mandatory advancement provision. The court first noted "a board's decision to accept an undertaking and to advance expenses is left to the business judgment of the board in the absence of a by-law specifically providing for mandatory advancement." In the context of advancing particular litigation expenses, and on a preliminary injunction record, the court found plaintiffs likely would succeed in rebutting the presumption of the business judgment rule because the defendant directors "fail[ed] to consider the potential magnitude of expenses or damages or the ability of the defendant directors to repay any funds ultimately advanced." In fact, the defendant directors failed to present evidence "rebutting plaintiffs' claim that the defendant directors failed to obtain or consider any information pertaining to [that] decision...."[87]

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[86] *Underbrink*, 2008 WL 2262316 at *11.

[87] *Underbrink*, 2008 WL 2262316 at *11 (citations and footnotes omitted).

The simple point, therefore, is that if a company does not have a mandatory indemnification bylaw, any decision by a corporate board to indemnify a director will be subject to the board's fiduciary duties and business judgment. But if the corporation *does* have a mandatory indemnification bylaw, the directors' business judgment is not implicated regarding the payment itself and indemnification would be required just like the terms of any other contract.[88] Similarly, in the absence of a bylaw provision making reimbursement of proxy expenses mandatory, any decision by corporate directors to reimburse proxy expenses, whether incurred by incumbent directors[89] or candidates nominated by shareholders who are elected to the board,[90] would also require the exercise of directors' business judgment. But, like a mandatory indemnification bylaw, if a corporation has a bylaw requiring the mandatory reimbursement of proxy expenses, the directors' would not be called upon to exercise any discretion on the payment itself.

In any event, caselaw raising questions regarding directors' exercise of discretion to authorize the reimbursement

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[88] *Cf. Havens*, 1997 WL 55957 at *13 ("[A] board's decision to accept an undertaking and to advance expenses is left to the business judgment of the board *in the absence of* a by-law specifically providing for mandatory advancement." (original emphasis deleted, emphasis supplied))

[89] *See Hall*, 171 A. 226 at 227.

[90] *See Steinberg*, 90 F. Supp. at 605.

of proxy solicitation expenses involve concerns wholly inapplicable in this case. In *Hall*, for example, the Chancery Court distinguished between proxy expenses incurred in connection with elections involving debates over corporate policy, and expenses incurred by incumbent directors solely for the self-interested purpose of retaining office. After considering caselaw establishing that reimbursement in the former situation would be appropriate and in the latter would not, the Chancery Court explained: "The nature of the contest must be looked at to see if it is one where it can be said that only the selfish desires of incumbent directors to hold on to their positions are at stake. If so, the persons who seek simply to procure their own re-election should pay the bills contracted in such a purely personal enterprise."[91] Where the corporation is called upon to repay the solicitation expenses incurred on behalf of shareholder-nominated directors, the concerns expressed by the court in *Hall* have no application. In making such reimbursement, there simply is, by definition, no danger that the incumbent directors would authorize the expenditure of such corporate funds for no reason but their own self-preservation. CA's concern, therefore, that the Bylaw, if adopted, would somehow deprive the incumbent directors of an ability to decide whether an proxy

[91] *Hall*, 171 A. at 229.

campaign of a shareholder-nominated director was based on *bona fide* policy issues is completely misplaced.

c. CA's Certificate Of Incorporation Does Not Bar AFSCME's Proposed Bylaw.

Article SEVENTH, Section 1 of CA's Certificate of Incorporation provides that "[t]he management of the business and the conduct of the affairs of the corporation shall be vested in the Board of Directors." CA argues that this provision renders unlawful any bylaw that might restrict the directors' managerial discretion.[92] CA is wrong.

Article SEVENTH of CA's certificate merely mirrors Section 141(a) of the DGCL, which simply provides that *if* a company's certificate of incorporation provides for the company to be managed by someone other the board of directors, the company shall be managed in accordance with the instructions in the certificate.[93] It does not, however, prevent the CA Board from compliance with the terms of the Company's bylaws. In other words, if a bylaw is valid under Section 109, the fact that CA's certificate vests in the Company's Board of Directors the responsibility to manage the business and affairs of the corporation does not mean that the Board is free to disregard the bylaws if they think their "discretion" requires them to do so.

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[92] RLF Opinion at 9-10.

[93] 8 Del. C. § 141(a)

CA, of course, will argue that Article SEVENTH does not excuse the Board's compliance with *all* bylaws, but only those bylaws adopted by shareholders that the Board believes would impinge on the directors' managerial "discretion." CA's argument in this regard, however, is fatally flawed. As discussed above,[94] Section 109(a) specifically vests in the shareholders the authority to adopt and amend bylaws, and even if this right is granted to the directors in a specific provision in the company's certificate, "[t]he fact that such power has been so conferred upon the directors ... shall not divest the stockholders or members of the power, nor limit their power to adopt, amend or repeal the bylaws."[95] To the extent, therefore, that CA suggests that the managerial authority granted to the Company's Board under Article SEVENTH somehow limits the shareholders' ability to adopt bylaws, such an interpretation would violate Section 109(a).[96]

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[94] *Supra* at Sec. III.A.3.b.

[95] 8 Del. C. § 109(a).

[96] But even if the Court determines that Article SEVENTH does, somehow, theoretically impose substantive limitations on the ability of CA's shareholders to adopt and amend bylaws (and it should not), the Court should still uphold the validity of the proposed Bylaw here because Article SEVENTH does not *clearly and unambiguously* prevent CA's shareholders from adopting bylaws relating to election procedures. *See generally Centaur Partners*, 582 A.2d at 927 ("There exists in Delaware a general policy against disenfranchisement ... Therefore, high vote requirements which purport to protect minority shareholders by disenfranchising the majority, must be clear and unambiguous.") (internal quotations and citations omitted).

V. CONCLUSION

For the foregoing reasons, AFSCME respectfully submits that the certified questions should be answered as follows:

(I) Is the AFSCME Proposal a proper subject for action by shareholders as a matter of Delaware law?

Yes.

(II) Would the AFSCME Proposal, if adopted, cause CA to violate any Delaware law to which it is subject?

No.

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Respectfully submitted,

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