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INVESTORS BANCORP: THE ROADS NOT TAKEN AND HOW TO MITIGATE THE CONSEQUENCES

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I. INTRODUCTION

In *In Re Investors Bancorp, Inc. Stockholder Litigation*[1] ("*Investors Bancorp*"), the Delaware Supreme Court announced that director compensation plans, in which directors have discretion to grant themselves equity, will be reviewed under the exacting "entire fairness" standard.[2] Prior to the Delaware Supreme Court's decision, the Delaware Court of Chancery held that compensation plans which (i) contained director-specific, "meaningful limits," and (ii) were approved by a majority of the fully informed, uncoerced, disinterested stockholders were subject to the more deferential business judgment standard of review.[3] The Delaware Supreme Court's decision effectively rejects this precedent.[4]

Additionally, the decision increased the ability of shareholder plaintiffs to enmesh Delaware corporations and their directors in costly litigation. Even where directors have received prior approval from stockholders of compensation plans that give directors discretion on how much to award themselves, director defendants will have the burden of proving *ab initio* that such plans are entirely fair to the corporation.[5] The Delaware Supreme Court noted that it balanced the "utility of the ratification defense and the need for judicial scrutiny of certain self-interested discretionary acts by directors,"[6] but ultimately determined that it cannot permit stockholder ratification to foreclose equitable review.[7]

Although the Delaware Supreme Court decided that entire fairness

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[1] *In re* Inv'rs Bancorp, Inc. Stockholder Litig., 177 A.3d 1208 (Del. 2017).

[2] *See id.* at 1211.

[3] *See id.* (citing Seinfeld v. Slager, No. 6462–VCG, 2012 WL 2501105, at *12 (Del. Ch. June 29, 2012)); *see also* Calma *ex rel.* Citrix Sys., Inc. v. Templeton, 114 A.3d 563, 569 (Del. Ch. 2015) (holding that the stockholder approval did not "bear[] specifically on the magnitude of compensation to be paid to its non-employee directors"). The Delaware Supreme Court has summarized the business judgment rule as,

> a "presumption that in making a business decision the directors of a corporation acted on an informed basis, in good faith and in the honest belief that the action taken was in the best interests of the company." A hallmark of the business judgment rule is that a court will not substitute its judgment for that of the board if the latter's decision can be "attributed to any rational business purpose."

Unocal Corp. v. Mesa Petrol. Co., 493 A.2d 946, 954 (Del. 1985) (citation omitted).

[4] *In re Inv'rs Bancorp*, 177 A.3d at 1212.

[5] *Id.* at 1211.

[6] *Id.*

[7] *Id.* at 1223.

continued . . .

governs the types of compensation plans at issue, the Delaware Supreme Court could have chosen alternate roads in its decision. *Investors Bancorp* involved colorable claims of waste and breach of the duty of disclosure.[8] The Delaware Supreme Court could have traveled down either or both of these roads to invalidate the directors' excessive compensation, rather than promulgating a new rule that discretionary director compensation plans are *always* subject to entire fairness.

This Article discusses the *Investors Bancorp* decision, the alternate roads the Delaware Supreme Court could have selected to invalidate the compensation plan, and the consequences of subjecting discretionary compensation plans to the exacting entire fairness standard of review *ab initio*. Part II summarizes the facts of *Investors Bancorp* and analyzes the legal rule promulgated by the decision. Part III examines waste and the disclosure issue as alternatives to the ultimate ruling. Finally, Part IV discusses the consequences of the decision and how courts should mitigate them.

II. THE *INVESTORS BANCORP* DECISION

A. The Facts

Investors Bancorp afforded the Delaware Supreme Court the opportunity to address director self-compensation plans for the first time since its prior decisions in *Kerbs v. California Eastern Airways, Inc.*[9] and *Gottlieb v. Heyden Chemical Corp.*[10] In *Investors Bancorp*, the Delaware Supreme Court reviewed an equity compensation plan (the "EIP"), which set forth that "[the] maximum number of shares that may be issued or delivered to all non-employee directors, in the aggregate, pursuant to the exercise of stock options or grants of restricted stock units . . . " was to be 30% of all options or restricted stock shares available for awards, all of which could have been granted in any calendar year.[11] As for directors who were employees of the corporation, the plan's limits on the available stock grants were "[a] maximum of 4,411,613 shares, in the aggregate . . . to any one employee . . ." and "[a] maximum of 3,308,710 shares, in the aggregate . . . to any one employee as a restricted stock or restricted stock unit grant."[12]

[8] *Id.* at 1212, 1215–16, 1224–26 (explaining how plaintiffs alleged that directors breached their fiduciary duties by granting themselves unfair and excessive awards after stockholders approved an Equity Incentive Plan).

[9] *See id.* at 1212, 1215–16, 1224–26; *see also* Kerbs v. California E. Airways, Inc., 90 A.2d 652, 660 (Del. 1952).

[10] Gottlieb v. Heyden Chem. Corp., 90 A.2d 660, 663 (Del. 1952).

[11] *In re Inv'rs Bancorp*, 177 A.3d at 1214 (alteration in original).

[12] *Id.* (alteration in original).

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Ultimately, the EIP left it to the discretion of the directors to allocate themselves up to 30%, in the aggregate, of all option or restricted stock shares available.[13]

In *Investors Bancorp*, the director defendants were comprised of (i) ten non-employee directors, and (ii) two executive directors.[14] The average annual compensation for the non-employee directors was $133,340, which ranged from $97,200 to $207,005.[15] In 2014, Kevin Cummings, the corporation's President, CEO, and one of the abovementioned executive directors, received annual compensation consisting of a base salary of $1,000,000, along with cash incentives, and benefits valued at $278,400, which totaled $2,778,770.[16] Domenick A. Cama, the corporation's COO, Senior Executive Vice President, and the other abovementioned executive director, received an annual compensation consisting of a base salary of $675,000, along with cash incentives, and benefits valued at $180,794, which totaled $1,665,794.[17]

The board set forth the details of the EIP referenced above and the reasoning behind it in the corporation's proxy statement, which was sent to stockholders prior to the annual meeting.[18] According to the proxy, "[t]he number, types and terms of awards to be made pursuant to the [EIP] are subject to the discretion of the Committee and have not been determined at this time, and will not be determined until subsequent to stockholder approval."[19] The proxy also stated that the EIP was intended to:

> [P]rovide[] additional incentives for [the Company's] officer's, employees and directors to promote [the Company's] growth and performance and to further align their interests with those of [the Company's] stockholders . . . and give [the Company] the flexibility [needed] to continue to *attract*, motivate and retain highly-qualified officers, employees and directors.[20]

At the corporation's annual meeting on June 5, 2015 , an overwhelming 96.25% of the voting shares approved the EIP.[21]

Just three days after stockholder approval of the EIP, the board

[13] *See id.* at 1212.
[14] *Id.*
[15] *Id.*
[16] *Id.* at 1213.
[17] *Id.*
[18] *See id.* at 1214.
[19] *Id.* (alteration in original).
[20] *Id.* at 1214 (alteration in original) (emphasis added).
[21] *Id.* Such percentage represented 79.1% of the total shares outstanding. *Id.*

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formed a compensation committee.[22] The committee consulted with outside counsel and compensation experts during four separate meetings regarding the awarding of the restricted stock and stock options contemplated by the EIP.[23] Ultimately, the board awarded themselves 7.8 million shares.[24] Non-employee directors' awards averaged $2,159,400 and totaled $21,594,000.[25] The Delaware Supreme Court observed that peer companies' non-employee awards averaged $175,817; thus, the company's awards were roughly twelve times those of its peers.[26] Cummings and Cama, the two executive directors, received stock options and restricted shares valued at $16,699,999 and $13,359,998, respectively.[27] Their awards were 1,759% and 2,571% higher than the averages of peer companies.[28]

Shortly after the awards were made public, stockholders filed complaints in the Delaware Court of Chancery alleging breaches of fiduciary duty by the directors for awarding themselves excessive compensation.[29] Relying on court of chancery precedent, Vice Chancellor Joseph R. Slights III granted the director defendants' motions to dismiss.[30] The plaintiffs appealed to the Delaware Supreme Court.[31]

B. The Delaware Supreme Court's Analysis

On appeal, the Delaware Supreme Court initiated its legal analysis by briefly referencing Section 141(h) of the General Corporation Law of the State of Delaware (the "DGCL").[32] Under Section 141(h), "[u]nless otherwise restricted by the certificate of incorporation or bylaws, the board of directors shall have the authority to fix the compensation of directors."[33] Although the Delaware Supreme Court does not delve into it, Section 141(h) has a bit of history.

Prior to the Delaware legislature's enactment of Section 141(h) in 1969, Delaware courts opined that directors "have no right to

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[22] *Id.*
[23] *Id.* at 1214–15.
[24] *Id.* at 1215.
[25] *Id.*
[26] *Id.*
[27] *Id.* at 1216.
[28] *Id.*
[29] *Id.*
[30] *In re* Inv'rs Bancorp, Inc. Stockholder Litig., No. 12327–VCS, 2017 WL 1277672, at *1 (Del. Ch. Apr. 5, 2017).
[31] *In re Inv'rs Bancorp*, 177 A.3d at 1211.
[32] *Id.* at 1217.
[33] DEL. CODE ANN. tit. 8, § 141(h) (2015).

continued . . .

compensation for their services . . . unless it is authorized by the charter, by-laws, or the stockholders."[34] In *Cahall v. Lofland*, stock was issued to directors as compensation for their services rendered and as commissions for selling its stock.[35] The Delaware Court of Chancery found, and the Delaware Supreme Court ultimately affirmed, that directors were not to be compensated unless otherwise provided for in the corporation's charter, by-laws, or by its stockholders.[36] The court of chancery reiterated this principal shortly thereafter in *Finch v. Warrior Cement Corp.*[37]

In the early twentieth century, the concept of corporate directors serving *gratis* was not a novel concept in Delaware, as courts in other jurisdictions also recognized that directors traditionally worked for free.[38] Typically, directors only received nominal fees for their attendance at board meetings.[39] As the twentieth century progressed, however, it became more common for corporate directors to receive compensation in some form or another.[40] To this end, in 1969, the Delaware legislature enacted Section 141(h), thereby enabling directors to set their own compensation.[41]

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[34] Lofland v. Cahall, 118 A. 1, 3 (Del. 1922).

[35] Cahall v. Lofland, 114 A. 224, 230 (Del. Ch. 1921), *aff'd*, 118 A. 1 (Del. 1922).

[36] *Lofland*, 118 A. at 8.

[37] Finch v. Warrior Cement Corp., 141 A. 54, 63 (Del. Ch. 1928).

[38] *See, e.g.*, Holms v. Republic Steel Corp., 69 N.E.2d 396, 402 (Ohio C.P. 1946) ("Directors of corporations, however, usually serve without wages or salary. They are generally financially interested in the success of the corporation they represent, and their service as directors secures its reward in the benefit which it confers upon the stock which they own."), *aff'd in part, rev'd in part on other grounds*, 84 N.E.2d 396 (Ohio Ct. App. 1949).

[39] *See* Charles M. Elson, *Director Compensation and the Management-Captured Board – The History of a Symptom and a Cure*, 50 SMU L. REV. 127, 138 (1996) (noting that directors often received nominal payment for attending board meetings, usually in the form of a gold double eagle). For a lengthy and robust discussion on the history of director compensation, see *id.*

[40] *Id.* Indeed, in 2015, the average compensation of directors of the top 200 companies in the financial industry was $280,000. Steven Hall & Partners, *2015 Director Compensation Study*, STEVEN HALL PARTNERS: EXECUTIVE COMPENSATION, http://www.shallpartners.com/wp-content/uploads/2015/09/SHP-2015-Director-Compensation-Study.pdf, 6 (last visited Apr. 21, 2018). *But see* Berkshire Hathaway Inc., Proxy Statement Pursuant to Section 14(a) of the Securities Exchange Act of 1934 (Form 14A) 6 (Mar. 17, 2017) (revealing that Berkshire Hathaway's non-employee directors receive an annual compensation of a paltry $4,200, on average, in 2016).

[41] *See* S. SAMUEL ARSHT & WALTER K STAPLETON, THE 1969 AMENDMENTS TO THE DELAWARE CORPORATION LAW 350 (1969). "[Section 141(h)] was intended to lay to rest a suggestion by way of dictum in an early case that directors are not empowered to vote compensation for members of the board unless authorized by a

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Although the DGCL empowers directors to set their own compensation, the Delaware Supreme Court held in *Investors Bancorp* that the board's determination to do so will "lie outside the business judgment rule's presumptive protection . . . [and is] subject to an affirmative showing that the compensation arrangements are fair to the corporation."[42] Historically, however, if a board's decision is ratified by the corporation's fully informed, uncoerced, and disinterested stockholders, that decision was reviewed under the business judgment standard of review, rather than entire fairness.[43] The Delaware Supreme Court then continued with a fulsome discussion of stockholder ratification in the context of director compensation plans.[44]

The Delaware Supreme Court observed that Delaware courts have recognized the stockholder ratification defense in three scenarios: (i) specific director awards; (ii) self-executing plans; and (iii) when directors exercised discretion and determined the amounts and terms of the awards.[45] Specific awards are just that: a defined number of shares.[46] And self-executing plans are those where the directors have "no discretion when making the awards."[47] Such plans are typically based on a pre-determined formula.[48] The Delaware Supreme Court

vote of stockholders or by a specific charter of by-law provision." *See id.* (alteration in original). *But cf.* N.Y. BUS. CORP. LAW § 505(d) ("The issue of such rights or options to one or more directors, officers or employees of the corporation or a subsidiary or affiliate thereof, as an incentive to service or continued service with the corporation, a subsidiary or affiliate thereof, or to a trustee on behalf of such directors, officers or employees, shall be authorized as required by the policies of all stock exchanges or automated quotation systems on which the corporation's shares are listed or authorized for trading, or if *the corporation's shares are not so listed or authorized, by a majority of the votes cast at a meeting of shareholders by the holders of shares entitled to vote thereon, or authorized by and consistent with a plan adopted by such vote of shareholders*." (emphasis added)).

[42] *In re* Inv'rs Bancorp, Inc. Stockholder Litig., 177 A.3d 1208, 1217 (Del. 2017) (alteration in original) (quoting Texlon Corp. v. Meyerson, 802 A.2d 257, 262 (Del. 2002)).

[43] *See e.g.*, *In re* 3Com Corp. S'holders Litig., No. C.A. 16721, 1999 WL 1009210, at *3 (Del. Ch. Oct. 25, 1999) ("Directors' decisions administering a shareholder approved [compensation plan] consistently with the plan are entitled to the protection of the business judgment rule." (alteration in original)); *see also* MICHAEL S. SIRKIN & LAWRENCE K CAGNEY, EXECUTIVE COMPENSATION §11.01(3) (2006) ("Putting the [compensation plan] to shareholders for approval should relieve any concern regarding self-dealing . . . ." (alteration in original)).

[44] *See In re Inv'rs* Bancorp,177 A.3d at 1217–18.

[45] *Id.* at 1222.

[46] *See id.* at 1217–19 ("[D]irectors could successfully assert the ratification defense when the stockholders were fully informed and approved stock option plans containing specific director awards.").

[47] *Id.* at 1222.

[48] *See id.* at 1211.

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was not concerned with those two scenarios because, in its view, they "present no real problems."[49] However, self-executing plans offer less flexibility to corporations in compensating their directors and officers. They also present other issues as it relates to proxy advisory firms and institutional investors and their jockeying with corporate stewards on compensation matters. This Article does not address these issues. In its analysis and discussion of prior case law, the Delaware Supreme Court affirmed the holdings of the prior Delaware Supreme Court cases, *Kerbs* and *Gottlieb*, that stockholder ratification is a valid defense where director awards are specific in amount and value, i.e., scenarios (i) and (ii) above.[50]

Next, the Delaware Supreme Court addressed the court of chancery cases applying the ratification defense to discretionary director self-compensation plans.[51] Notably, in *In re 3Com Corporation Shareholders Litigation*,[52] the court of chancery approved stockholder ratification of option grants that contained director specific ceilings.[53] But in *Sample v. Morgan*,[54] in invalidating stockholder ratification, the court of chancery explained that "Delaware . . . does not embrace a 'blank check' theory, [notwithstanding stockholder ratification]."[55] There, the two non-employee directors on the compensation committee awarded *all* 200,000 shares contemplated by the stockholder-approved plan to the three employee directors.[56] Recently, in *Calma ex rel. Citrix Systems, Inc. v. Templeton*,[57] Chancellor Andre Bouchard explained, while striking down a stockholder approved discretionary compensation plan, for such plans to be subject to the business judgment rule they must have "meaningful limits," in addition to being director-specific.[58] In sum, the case law leading up to *Investors Bancorp* held that so long as discretionary option plans had "director-specific," "meaningful limits," and did not appear to be a blank check authorization, such plans that were approved by stockholders would be subject to business judgment.

The apparent disparity between compensation awards of the

[49] *Id.* at 1222.

[50] *Id.* at 1217–19.

[51] *See id.* at 1219–20.

[52] *See In re* 3COM Corp. S'holders Litig., No. C.A. 16721, 1999 WL 1009210 (Del. Ch. Oct. 25, 1999).

[53] *Id.* at *3.

[54] *See* Sample v. Morgan, 914 A.2d 647 (Del. Ch. 2007).

[55] *Id.* at 663 (alteration in original).

[56] *Id.* at 650–51.

[57] *See* Calma *ex rel.* Citrix Sys., Inc. v. Templeton, 114 A.3d 563 (Del. Ch. 2015).

[58] *See id.* at 578, 588.

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directors of Investors Bancorp and those of their peers, in addition to the court of chancery's struggle to reconcile discretionary plans and its own precedent, prompted the Delaware Supreme Court to withdraw stockholder ratification as a tool in shifting the review of discretionary compensation plans to the business judgment rule.[59] It begs the question that, if the Investors Bancorp directors had awarded themselves compensation in line with peers in their industry, would the Delaware Supreme Court would have chosen the road it did?

Regardless, the avenue the Delaware Supreme Court did select was that "when it comes to discretion, directors' exercise following stockholder approval of an equity incentive plan, ratification cannot be used to foreclose the court of chancery from reviewing those further discretionary actions when a breach of fiduciary duty claim has been properly alleged."[60] In reaching its conclusion, the Delaware Supreme Court held that "when stockholders have approved an equity incentive plan that gives directors discretion to grant themselves awards within *general parameters* . . . [then] the directors will be required to prove the fairness of the awards to the corporation."[61] Some commentators have parsed this language to suggest that if plans articulate more *specific* parameters, then perhaps stockholder ratification will cause such plans to be subject to the business judgment standard of review.[62] This observation is likely wishful thinking, as Delaware courts unsuccessfully applied a meaningful limits requirement.[63] Ultimately, notwithstanding stockholder ratification, discretionary incentive plans with director specific, meaningful limits may be subject to corporate law's most exacting standard of review: entire fairness.[64]

III. The Roads Not Taken: Waste and Disclosure

The Delaware Supreme Court is often inclined to narrow its decision to the facts of the case at hand.[65] However, the Delaware Supreme

[59] *See* Inv'rs Bancorp, Inc. Stockholder Litig., 177 A.3d 1208, 1222–25 (Del. 2017).

[60] *Id.* at 1222.

[61] *Id.* at 1211 (alteration in original) (emphasis added).

[62] *See, e.g.*, James E. Earle et al., *Delaware Supreme Court Shines a (Blurry) Spotlight on Director Compensation Decisions: In Re Investors Bancorp, Inc. Stockholder Litigation*, K&L Gates (Jan. 17, 2018), http://www.klgates.com/delaware-supreme-court-shines-a-blurry-spotlight-on-director-compensation-decisions-in-re-investors-bancorp-inc-stockholder-litigation-01-17-2018/.

[63] *See Calma ex rel. Citrix Sys.*, 114 A.3d at 585.

[64] *See In re Inv'rs Bancorp*, 177 A.3d at 1217.

[65] *See, e.g.*, Delaware State Univ. Chapter of Am. Ass'n of Univ. Professors v. Delaware State Univ., 813 A.2d 1133, 1139 (Del. 2003) ("We note that this decision

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Court's decision not to limit its holding to the colorable waste and disclosure issues in this case evidences a consensus of the Delaware Supreme Court to shift the standard of review for discretionary incentive plans that obtain stockholder approval from business judgment to entire fairness.[66] However, it seems apparent from the decision that the Delaware Supreme Court aspired for a permanent fix for these types of cases.[67]

A. Waste

Most corporate law treatises suggest that the task of proving a corporation has committed waste is a fruitless endeavor.[68] It is an eleventh-hour salvo when plaintiffs are cornered into the business judgment standard of review. Typical "compensation claims, alleging that particular compensation was excessive and thereby constituted corporate waste, have not fared well under Delaware law. Most . . . are dismissed at the pleading stage."[69] Waste, in the traditional sense, occurs when:

> [W]hat the corporation has received is so inadequate in value that no person of ordinary, sound business judgment would deem it worth what the corporation has paid. If it can be said that ordinary businessmen might differ on the sufficiency of the terms, then the court must validate the transaction.[70]

The foregoing definition is quite deferential to the decision making of the board. That is why lawyers, judges, and scholars believe that

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is a narrow holding confined to the facts of this case.").

[66] *Compare id.*, *with In re Inv'rs Bancorp,* 177 A.3d at 1217.

[67] *See In re Inv'rs Bancorp,* 177 A.3d at 1222–23.

[68] *See, e.g.*, 1 R. FRANKLIN BALOTTI & JESSE A. FINKELSTEIN, THE DELAWARE LAW OF CORPORATIONS AND BUSINESS ORGANIZATIONS § 4.11[A], at 4–49 (3d ed. 2017) ("Plaintiffs rarely satisfy the waste standards."). *But see In Re* Citigroup Inc. S'holder Derivative Litig., 964 A.2d 106, 111–12, 138 (Del. Ch. 2009) (illustrating the court of chancery denying a motion to dismiss in which plaintiffs alleged that an executive compensation package of $68 million for a departing CEO was waste).

[69] Rudolf Koch & Christopher H. Lyons, *Delaware Insider: Executive Compensation Lessons from Freedman v. Adams*, BUS. LAW. TODAY (March 2013), http://www.americanbar.org/publications/blt/2013/03/delaware_insider.html (last visited Jan. 10, 2017).

[70] Saxe v. Brady, 184 A.2d 602, 610 (Del. Ch. 1962). For an in-depth discussion on corporate waste, *see generally* Harwell Wells, *The Life (and Death) of Corporate Waste*, 74 WASH. & LEE L. REV. 1239, 1239 (2017) (discussing "the origin of corporate waste, documents and explains its survival, and tentatively foresees its demise").

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plaintiffs are almost certain to lose on their claims of waste.[71]

Perhaps this is why the Delaware Supreme Court in *Investors Bancorp* felt it had to limited stockholder ratification of compensation plans to only those where directors retain discretion. As explained, the reason the Delaware Supreme Court could not permit review of discretionary compensation plans, that stockholders approved to continue under the business judgment standard of review, is because egregious cases of excessive compensation would be insulated from judicial review.[72]

Waste, however, is not as elusive as commentators have proclaimed it to be[73] and defeats the ratification issue by preserving judicial review of such cases. One does not have to look further than previous director compensation cases to find examples of when plaintiffs satisfied the waste pleading and survived the motion to dismiss stage.[74] Notwithstanding waste's poor reputation, the Delaware Supreme Court could have relied on prior precedent and the waste doctrine to invalidate the compensation plan here.[75]

Two cases are illustrative on this point: *Lewis v. Vogelstein*[76] and *Sample v. Morgan*.[77] In *Lewis*, the stockholder-approved director

[71] Earle et al., *supra* note 62.

[72] *See In re Inv'rs Bancorp*, 177 A.3d at 1222–23.

[73] *See e.g.*, Todd A. Murray & Lyndon F. Bittle, *Emerging Issues Raised by Derivative Shareholder Actions Involving Foreign Corporations Headquartered in Texas*: *Making Sense of the Interaction Between Texas Procedures and Substantive Law*, 39 TEX. TECH. L. REV. 1, 12 (2006).

[74] *See generally* Sample v. Morgan, 914 A.2d 647 (Del. Ch. 2007) (pleading sufficiently alleged waste and motion to dismiss was not granted); Lewis v. Vogelstein, 699 A.2d 327 (Del. Ch. 1997) (alleging corporate waste and surviving the motion to dismiss stage).

[75] Traditionally, the Delaware Supreme Court has limited its review to issues raised at the trial level. *See, e.g.*, DEL. CT. R. 8. Here, the plaintiff did not plead waste in the court of chancery or in its brief to the Delaware Supreme Court; however, the Delaware Supreme Court could have reviewed the claim *sua sponte* in the interests of more case-specific issues and justice. *See* DFC Global Corp. v. Muirfield Value Partners, L.P., 172 A.3d 346, 363 (Del. 2017) ("We place great value on the assessment of issues by our trial courts, and it is not only unwise, but unfair and inefficient, to litigants and the development of the law itself, to allow parties to pop up new arguments on appeal they did not fully present below. For that reason alone, we are reluctant to even consider this argument. *Nonetheless*, because of its relationship to more case-specific issues, we explain why, even if this were fairly presented, DFC has not persuaded us to adopt its position." (emphasis added)); Bank of Delaware v. Claymont Fire Co. No. 1, 528 A.2d 1196, 1199 (Del. 1987) ("The form of pleadings should not place a limitation upon the court's ability to do justice.").

[76] *See Lewis*, 699 A.2d at 327.

[77] *See Sample*, 914 A.2d at 647.

continued . . .

compensation plans were self-executing (i.e., the second scenario).[78] The plan provided for one-time grants of 15,000 options per director and annual grants depending on the specific director's tenure: outside directors with five or fewer years of service would qualify for no more than 5,000 shares, while those with more than five years of services would qualify for up to 10,000 shares.[79] In denying the defendants' motion to dismiss on the claim of waste, Chancellor Allen observed that allegations of waste are inherently factual and in need of more evidentiary analysis.[80] He also noted, however, there are certain situations where one would not need further factual findings to dismiss a claim of waste.[81]

In *Sample*, the stockholder-approved plans were discretionary in nature (i.e., those of the third scenario where directors retain discretion in awarding themselves options).[82] The option plan in that case limited the number of options directors could award themselves to 200,000 shares.[83] Similar to *Investors Bancorp*, the incentive plan's purported goal was to enable the company to "attract[] and retain[] key employees."[84] Within hours of the annual meeting, however, the board formed a compensation committee to administer the plan, in which *all* 200,000 shares would be issued.[85] Thus, stockholders were allegedly led to believe the grants would be made over time to a more diffuse group of employees.[86]

In finding that the plaintiffs pled facts to support a pleading-stage inference of waste, then-Vice Chancellor Strine, now Chief Justice, noted that "[w]hen pled facts support an inference of waste, judicial nostrils smell something fishy and full discovery into the background of the transaction is permitted."[87] He explained that plaintiffs are permitted to move past the pleadings stage "when the motivations for a transaction are unclear by pointing to economic terms so one-sided as to create an inference that no person acting in a good faith pursuit of the corporation's interests could have approved the terms."[88]

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[78] *See Lewis*, 699 A.2d at 329; *see also* Inv'rs Bancorp, Inc. Stockholder Litig., 177 A.3d 1208, 1219 (Del. 2017) (explaining that the plans in *Lewis* were "self-executing, meaning that no further director action was required to implement the awards as they were earned").

[79] *See Lewis,* 699 A.2d at 329–330.

[80] *See id.* at 339.

[81] *See id.*

[82] *See Sample*, 914 A.2d at 654–56.

[83] *See id.* at 650–51.

[84] *Id.* at 662 (alteration in original).

[85] *See id.* at 657 (emphasis added).

[86] *See id.* at 666–67.

[87] *Id.* at 670.

[88] *Id.*

continued . . .

Under this analysis, the piscine nature of the value and timing of the options in *Investors Bancorp* would seem to warrant wading into full discovery. The economic terms of the option plan suggest a pleading-stage inference of waste.[89] The two executive directors of Investors Bancorp granted themselves options that were worth 1,759% and 2,571% times those of executive directors at peer companies.[90] And the non-employee directors awarded themselves options averaging $2,159,400, while those at peer companies received on average $175,817.[91] Like the options in *Sample*, which Vice Chancellor Strine acknowledged as "extraordinary,"[92] the options in *Investors Bancorp* are so out of the ordinary to suggest, at a minimum, waste at the pleading stage. Moreover, the interchangeable language in the proxies of *Sample* and *Investors Bancorp*, along with the quick turn-arounds to grant themselves options, suggests the motives were not to attract new employees but to compensate themselves for past performance. With such facts, the Delaware Supreme Court *could* have remanded the case back to the court of chancery and requested the parties to address the conspicuous issue of waste.

B. Disclosure

In order for stockholder ratification to be valid, stockholders must be fully informed of all material facts prior to voting.[93] The fiduciary duty of disclosure "obligates directors to provide stockholders with accurate and complete information material to a transaction or other corporate event that is being presented to them for action."[94] Directors

[89] *See In re* Inv'rs Bancorp, Inc. Stockholder Litig, 177 A.3d 1208, 1215–16 (Del. 2017).

[90] *Id.*

[91] *Id.* at 1215.

[92] *Sample*, 914 A.2d at 670.

[93] *See* Stroud v. Grace, 606 A.2d 75, 84 (Del. 1992) ("[The duty of disclosure] represents nothing more than the well-recognized proposition that directors of Delaware corporations are under a fiduciary duty to disclose fully and fairly all material information within the board's control when it seeks shareholder action." (alteration in original)); Lilia Volynkova, Note, Seinfeld v. Slager: *The Delaware Chancery Court's New Legal Standard for Reviewing Directors Decision About Their Own Pay,* 58 N.Y.L. SCH. L. REV. 741, 754 (2014) ("Another way for a stockholder-plaintiff to eliminate the protection of the business judgment rule given to a ratified director decision is to successfully allege that the proxy statement soliciting stockholder approval of the compensation plan was misleading or omitted material information.").

[94] Malone v. Brincat, 722 A.2d 5, 10 (Del. 1998). *See also* Malpiede v. Townson, 780 A.2d 1075, 1086 (Del. 2001) ("[T]he board's fiduciary duty of disclosure . . . are not independent duties but the application in a specific context of the board's fiduciary duties of care, good faith, and loyalty.").

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violate their duty to disclose when an alleged omission or misrepresentation is material.[95] Information is considered material to stockholders when "there is a substantial likelihood that a reasonable shareholder would consider it important in deciding how to vote."[96] In ratification cases where a breach of the duty of disclosure is raised, directors carry an affirmative "burden of demonstrating full and fair disclosure."[97]

The issue of disclosure in *Sample* arose in a similar context as *Investors Bancorp.* There, directors told stockholders via the proxy statement that the purpose of the incentive plan was to "advance the interests of the Company and its stockholders by providing a means of *attracting* and retaining *key employees* . . . by granting equity-based awards . . . which will be subject to vesting schedules based on the recipient's continued employment . . . ."[98] The directors' awarding themselves *all* 200,000 available options belied their statement to stockholders that the options were intended to "attract" new employees.[99] Vice Chancellor Strine explained the language used in the proxy was "deliberately designed to suggest that grants would be made over time to a more diffuse group of employees."[100] The foregoing divergence led Vice Chancellor Strine to conclude that the proxy was materially misleading and, therefore, the directors' ratification defense was invalid.[101]

In *Investors Bancorp*, the directors used similar language in the proxy to solicit stockholder ratification. There, the proxy stated that by approving the plan, "stockholders will give [the Company] the

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[95] *See, e.g.*, Arnold v. Soc'y for Sav. Bancorp, Inc., 650 A.2d 1270, 1277 (Del. 1994) ("The essential inquiry is whether the alleged omission or misrepresentation is material.").

[96] Rosenblatt v. Getty Oil Co., 493 A.2d 929, 944 (Del. 1985) (quoting TSC Indus., Inc. v. Northway, Inc., 426 U.S. 438, 449 (1976)); Richard A. Booth, *The Two Faces of Materiality*, 38 DEL. J. CORP. L. 517, 518 (2013) (citing *TSC Indus.,* 426 U.S. at 449) ("The information need not be so important that it would change the outcome, but it cannot be so trivial that it would not affect the total mix of available information.").

[97] *Sample*, 914 A.2d at 665 (quoting Loudon v. Archer-Daniels-Midland Co., 700 A.2d 135, 141 (Del. 1997)).

[98] *Id.* at 656 (quoting Second Amended Class Action and Derivative Complaint, Exhibit 1 at 4, Sample v. Morgan, 914 A.2d 647, 665 (Del. Ch. 2007) (C.A. No. 1214–N)). In *Sample*, other issues compounded this alleged misrepresentation. The directors had contracted not to issue any additional equity for five years. *Id.* at 657. Thus, they were granting themselves the last available equity for quite some time. The directors also failed to disclose that the company would be paying the taxes for any executives receiving stock under the incentive plan. *Id.* at 658.

[99] *See id.* at 666.

[100] *Id.* at 667.

[101] *Id.* at 668.

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flexibility [it] need[s] to continue to *attract*, motivate and retain highly qualified officers, employees and directors by offering a competitive compensation program that is linked to the performance of the [the Company's] common stock."[102] Additionally, directors told stockholders that "[t]he number, types and terms of awards . . . will not be determined until subsequent to stockholder approval."[103] The plaintiffs contended, and the Delaware Supreme Court seemed to agree, that such statements are forward-looking (i.e., "stockholders understood that the directors would reward Company employees for future performance, not past services.").[104] Lastly, similar to the directors in *Sample*, shortly after the annual meeting, directors held board meetings to disperse the newly-approved options to themselves.[105]

After discussing issues raised regarding disclosure and disparity between what the directors awarded themselves and those of directors at peer companies, the Delaware Supreme Court held "[t]hat plaintiffs have alleged facts leading to a pleading stage reasonable inference that the directors breached their fiduciary duties in making unfair and excessive discretionary awards to themselves after stockholder approval of the EIP."[106] The Delaware Supreme Court explained that "[b]ecause the stockholders did not ratify the specific awards the directors made under the EIP," they must prove that they were entirely fair.[107]

It is unclear from the Delaware Supreme Court's opinion whether it found a breach of the duty of disclosure, or at a minimum, an inference of a breach thereof at the pleadings stage. The Delaware Supreme Court simply stated that there was an inference of a breach of fiduciary duties in general.[108] Nonetheless, the Delaware Supreme Court could have narrowly held that, at the pleading stage, the directors did not carry their burden that the proxy "fairly and fully" disclosed the nature of the awards, therefore remanding the case back to the court of chancery on those grounds.[109]

[102] *In re* Inv'rs Bancorp, Inc. Stockholder Litig., 177 A.3d 1208, 1214 (Del. 2017) (alteration in original) (emphasis added).

[103] *Id.* at 1214. At the court of chancery level, Vice Chancellor Slights strictly interpreted the word "subsequent." *See In re* Inv'rs Bancorp, Inc., Stockholder Litig., No. CV 12327–VCS, 2017 WL 1277672, at *1 (Del. Ch. Apr. 5, 2017), *rev'd*, 177 A.3d 1208 (Del. 2017). Indeed, the awards were determined subsequent to stockholder ratification, albeit *days* afterward. *See id.* at 1214–15.

[104] *In re Inv'rs Bancorp*, 177 A.3d at 1224.

[105] *Id.* at 1214.

[106] *Id.* at 1224.

[107] *Id.*

[108] *Id.* at 1225.

[109] *In re* Inv'rs Bancorp, Inc., Stockholder Litig., No. CV 12327–VCS, 2017 WL 1277672, at *9 (Del. Ch. Apr. 5, 2017), *rev'd*, 177 A.3d 1208 (Del. 2017).

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In refusing to remand on those grounds, the Delaware Supreme Court most likely believed that Delaware courts had exhausted the development of case law on discretionary award plans and stockholder ratification thereof. In *Seinfeld v. Slager*, Vice Chancellor Glasscock set forth the requirement that putative incentive plans have "meaningful limits" rather than a blank check for the directors to award themselves compensation.[110] As discussed previously, in *Templeton*, Chancellor Bouchard determined stockholder ratification of a discretionary incentive plan failed because the proxy did not contemplate the magnitude of the awards to the non-employee directors and there were no director-specific "ceilings" like those in *3Com*.[111]

Indeed, at the court of chancery level, Vice Chancellor Slights found that the EIP complied with both the "director-specific" and "meaningful limit" requirements laid down in prior cases.[112] Notwithstanding the defendants' apparent compliance with such limits, the Delaware Supreme Court still determined there was an inference of a breach of fiduciary duties.[113] Following the Delaware Supreme Court's reasoning, had business judgment been the standard of review, it would have foreclosed a court from reviewing such breach.[114] Therefore, rather than fashioning an additional rule to be complied with, such as an arbitrary cap on the value or number of shares to be granted to directors, or confining its ruling to waste and/or disclosure, the Delaware Supreme Court definitively withdrew the use of stockholder ratification to shift the standard of review of such plans from entire fairness to business judgment.[115]

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[110] Seinfeld v. Slager, No. 6462–VCG, 2012 WL 2501105, at *12 (Del. Ch. June 29, 2012) ("Though the stockholders approved this plan, there must be some *meaningful* limit imposed by the stockholders on the Board for the plan to . . . receive the blessing of the business judgment rule . . . .").

[111] *See* Calma *ex rel* Citrix Sys., Inc. v. Templeton, 114 A.3d 563, 569 (Del. Ch. 2015); *see also In re* 3Com Corp. S'holders Litig., No. C.A. 16721, 1999 WL 1009210, at *6 (Del. Ch. Oct. 25, 1999).

[112] *In re* Inv'rs Bancorp, Inc. Stockholder Litig., C.A. No. 12327–VCS, 2017 WL 1277672, at *8 (Del. Ch. Apr. 5, 2017) ("In this case, stockholders approved specific limits and the directors then approved awards within the bounds of these limits. Accordingly, their decision must be reviewed for waste."), *rev'd*,177 A.3d 1208 (2017).

[113] *In re Inv'rs Bancorp*, 77 A.3d at 1225.

[114] *Id.* at 1222–23.

[115] *Id.* at 1211.

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IV. CONSEQUENCES OF THE DECISION

A. Immediate Impact on Director Compensation Decision Making

As it concerns director compensation plans, the most immediate consequence of *Investors Bancorp* is that directors will now have to determine whether the litigation risk associated with an action that may trigger the entire fairness standard of review is worth it.[116] Prior to the decision, so long as stockholders approved the board of directors' discretionary plan and there were no concerns raising the issues of waste or disclosure, directors were empowered to set appropriate compensation plans with meaningful limits without substantial fear of litigation.[117] The business judgment standard of review is a more deferential standard to corporate directors and the likelihood of a motion to dismiss being granted is significant, thus serving as an impediment to such suits. Because entire fairness is a more exacting standard of review, there is now substantial risk that suits involving director compensation will survive motions to dismiss, and as a result, Delaware corporations will be forced to expend more resources defending such cases.

Entire fairness, which is Delaware's strictest standard of review, "applies when the board of directors labors under actual conflicts of interest."[118] A board of directors' decision to compensate itself is such a conflict.[119]

Indeed, the entire fairness standard of review consists of two prongs: fair dealing and fair price.[120] The fair dealing prong "embraces [the] questions of when the transaction was timed, how it was initiated, structured, negotiated, disclosed to the directors, and how the approvals of the directors and the stockholders were obtained."[121] The fair price prong entails a court's analysis of the price and whether it falls on a

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[116] Earle et al., *supra* note 62.

[117] *Id.*

[118] *In re* Trados Inc. S'holder Litig., 73 A.3d 17, 44 (Del. Ch. 2013). *See also* Kahn v. M&F Worldwide Corp., 88 A.3d 635, 644 (Del. 2014) ("[E]ntire fairness is the highest standard of review in corporate law.").

[119] *See generally In re Investors Bancorp*, 77 A.3d at 1208 (discussing board of directors' award of compensation to itself). As discussed throughout this Article, prior to *Investors Bancorp*, directors were able to shift the standard of review regarding discretionary compensation plans to business judgment if they obtained stockholder approval and the plan complied with the requirements set forth by the court of chancery. *See id.* at 1211.

[120] *See, e.g.*, Weinberger v. UOP, Inc., 457 A.2d 701, 711 (Del. 1983) (applying entire fairness); BALOTTI & FINKELSTEIN, *supra* note 68, § 9.40, at 9–119 (discussing entire fairness in merger transactions).

[121] *Weinberger*, 457 A.2d at 711 (alteration in original).

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"range of reasonable values."[122] Although the two prongs likely will be examined separately, "the test for fairness is not a bifurcated one as between fair dealing and price."[123] Rather, it is a wholesome review of the two prongs intertwined together.[124] Without delving into the entire fairness line of cases, one can gather that the application of the entire fairness test requires a fulsome review of evidence, which usually requires lengthy discovery. The conclusion that entire fairness will be the applicable standard of review "is often of critical importance."[125] Delaware courts have long recognized that entire fairness is so exacting that a determination that it applies is often outcome determinative.[126] The burden of proving that a transaction is entirely fair is quite onerous. To determine whether the director defendants have met such burden as it pertains to a discretionary compensation plan will likely be "*impossible* by examining only the documents [a court] is free to consider on a motion to dismiss," i.e., the complaint and any documents it incorporates by reference.[127] Thus, the obvious conclusion is the requirement that entire fairness applied to discretionary compensation plans will almost always preclude a dismissal of a complaint at the motion to dismiss stage.[128] Because dismissing an entire fairness case at the motion to dismiss stage is quite rare, entire fairness is considered to be the most-friendly standard of review for plaintiffs.[129]

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[122] Cede & Co. v. Technicolor, Inc., No. Civ.A. 7129, 2003 WL 23700218, at *2 (Del. Ch. Dec. 31, 2003), *aff'd in part, rev'd in part on other grounds*, 884 A.2d 26 (Del. 2005).

[123] *Weinberger*, 457 A.2d at 711.

[124] *See id.*; Kahn v. Lynch Comm'n Sys., Inc., 669 A.2d 79, 84 (Del. 1995) (explaining that entire fairness "requir[es] an examination of all aspects of the transaction to gain a sense of whether the deal in its entirety is fair"); *see also In re* Dole Food Co. Stockholder Litig., No. 8703–VCL, No. 9079–VCL, 2015 WL 5052214, at *25 (Del. Ch. Aug. 27, 2015) (applying entire fairness to a controlling stockholder's take-private transaction).

[125] Kahn v. Lynch Comm'n Sys., Inc., 638 A.2d 1110,1116 (Del. 1994) (citing Nixon v. Blackwell, 626 A.2d 1366, 1376 (Del. 1993)).

[126] *See, e.g.*, AC Acquisitions Corp. v. Anderson, Clayton & Co., 519 A.2d 103, 111 (Del. Ch. 1986) ("Because the effect of the proper invocation of the business judgment rule is so powerful and the standard of entire fairness is so exacting, the determination of the appropriate standard of judicial review frequently is determinative of the outcome of derivative litigation."). *But see Nixon*, 626 A.2d at 1381 ("In a case such as this where the business judgment rule is not applicable and the entire fairness test is applicable, the imposition of the latter test is not, alone, outcome-determinative.").

[127] Orman v. Cullman, 794 A.2d 5, 20 n.36 (Del. Ch. 2002) (alteration in original) (emphasis added).

[128] *See id.* at 21.

[129] *E.g.*, Lewis H. Lazarus & Brett M. McCartney, *Standards of Review in Conflict Transactions on Motions to Dismiss: Lessons Learned in the Past Decade*, 36 DEL. J. CORP. L. 967, 974–75 (2011) ("Generally, where a plaintiff can plead

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Notwithstanding the onerous burden of proving entire fairness, there are procedural steps a Delaware corporation can take to ease this burden. To satisfy the fair dealing and fair price aspects, a board of directors can set up a compensation committee, which most publicly-traded corporations already employ.[130] In addition to the compensation committee, the board should consider seeking advice from an independent compensation consultant. The board should also consider examining compensation at peer companies and attempt to remain in those ranges because the Delaware Supreme Court in *Investors Bancorp* honed in on the disparity between the Investors Bancorp directors' awards and those at peer companies.[131] Additionally, as noted above, in an entire fairness analysis a court will examine how and when the directors disclosed the plan to stockholders when the directors sought stockholder approval.[132] The language used by the board in *Investors Bancorp* to describe why the options were to be awarded was misleading. If a board can specifically articulate an estimation of why and when the options will be employed, that will aid its case to prove entire fairness.

Even if a board is diligent in adhering to the above, there is no guarantee it can prevail at the motion to dismiss stage or otherwise. The difficult and expensive nature of defending an entire fairness case often leads to directors and corporations settling cases they might otherwise win on the merits.[133] Some practitioners have opined that the *Investors Bancorp* decision will not cause liabilities for directors and corporations unless the awards are excessive or other significant problems have occurred, such as inadequate or misleading disclosure.[134] However,

facts sufficient to have the transaction reviewed under entire fairness, the plaintiff's complaint will survive a motion to dismiss.").

[130] Barry J. Reiter, *The Role of Compensation Committees in Corporate Governance*, FINDLAW, http://corporate.findlaw.com/finance/the-role-of-compensation-committees-in-corporate-governance.html (last visited Mar. 19, 2018).

[131] *See In re* Inv'rs Bancorp, Inc. Stockholder Litig., 177 A.3d 1208, 1215–16 (Del. 2017).

[132] *See supra* Section III.A.

[133] *See, e.g.*, Robert S. Reder & Lauren Messonnier Meyers, *Delaware Supreme Court Affirms Pleading-Stage Dismissal of Control Stockholder Buyout Litigation*, 69 VAND. L. REV. EN BANC 17, 18–19 (2016) (explaining that in entire fairness cases, "[e]xcept in the most egregious cases, settlements involving the payment of attorneys' fees and the granting of universal settlements have been the usual outcome).

[134] *See* Gail Weinstein et al., *The Limits of Shareholder Ratification for Discretionary Director Compensation*, HARV. L. SCH. F. ON CORP. GOVERNANCE AND FIN. REG. (Dec. 21, 2017), https://corpgov.law.harvard.edu/2017/12/21/the-limits-of-shareholder-ratification-for-discretionary-director-compensation/ ("In our view, directors are unlikely to have liability for awards issued under discretionary plans unless the awards were excessive and/or there are other significantly

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potential plaintiffs and their attorneys are still incentivized to bring suits for the possibility of a settlement.

An illustrative example of this is the recent Facebook litigation, *Espinoza v. Zuckerberg*.[135] There, the shareholder plaintiff challenged Facebook's director equity compensation plan as excessive.[136] "Facebook ranked sixth of the twelve largest U.S. public companies [as measured] by market cap value."[137] At the same time, the average pay, of Facebook non-employee directors, which included cash and equity, was $386,000, ranking second of the twelve, with the average pay of the third and fourth ranked companies being slightly above that amount at $367,000 and $363,000, respectively.[138] While Facebook was one of the pack leaders, its compensation was certainly in a range observers would label as reasonable. The disparities of the director compensation, as compared to their peers in *Investors Bancorp*, were simply not present in *Espinoza.*[139] Nonetheless, this lack of apparent disparity did not prevent shareholder plaintiffs from targeting Facebook.[140]

When the directors of Facebook moved to dismiss the complaint, Chancellor Bouchard held entire fairness would apply to the compensation plan, thus requiring a more fulsome review of the evidence.[141] Subsequently, the case was settled.[142] In addition to the settlement cost, Chancellor Bouchard approved fees and expenses of an impressive $525,000 for plaintiff's attorneys.[143] *Espinoza* serves as a cautionary tale that even when directors keep close to the average compensation among their peer companies they still can end up in costly litigation and ultimately settle a case they likely would have won at trial. The $525,000 award for plaintiffs' attorneys combined with their

problematic factors (such as a flawed process or disclosure).").

[135] *See* Espinoza v. Zuckerberg, 124 A.3d 47 (Del. Ch. 2015).

[136] *Id.* at 52.

[137] *See* David E. Gordon, *Facebook Settlement: Litigation Over Director Compensation*, HARV. L. SCH. F. ON CORP. GOVERNANCE AND FIN. REG. (Mar. 10, 2016), https://corpgov.law.harvard.edu/2016/03/10/facebook-settlement-litigation-over-director-compensation/ (alteration in original).

[138] *Id.*

[139] *See supra* Part I.

[140] *See Espinoza*, 124 A.3d at 52 (showing shareholders filed a suit against Facebook despite differences between *Espinoza* and *Investors Bancorp*).

[141] *Id.* at 66 (showing that even though while *Espinoza* was pre-*Investors Bancorp*, Facebook did not comply with the statutory formalities in getting the plan approved by stockholder vote, which would have shifted the standard of review back to business judgment). Nonetheless, because it is a compensation case and the applicable standard of review is entire fairness it is illustrative of how such cases can result in the future. *See id.*

[142] *See* Gordon, *supra* note 137.

[143] *Id.*

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survival at the motion to dismiss stage may incentivize other shareholders and their attorneys to scrutinize proxy statements for director compensation that deviate from the median of similarly-situated companies.[144]

B. Mitigating the Practical Implications of *Investors Bancorp*

Although not inexorable in every case, because entire fairness will apply *ab initio* to discretionary compensation cases, the likely result is that the board of directors' decision to compensate themselves may require a full trial.[145] Dismissal at the motion to dismiss stage may be challenging and unlikely for the reasons mentioned above. Similarly, the entry of a final judgment, even after discovery on a motion for summary judgment, may also be challenging, as there likely will be unresolved questions of material facts regarding the two prongs of entire fairness.[146] As evident in the Facebook litigation, even in a case where it appears the facts are favorable to the defendants, director defendants may still end up at trial, assuming they do not settle.[147]

The Delaware Supreme Court has recognized these practical implications of the automatic requirement of an entire fairness review.[148] When the standard of review is entire fairness, the defendants retain the burden of persuasion.[149] In other words, the defendants will bear the burden of proving the discretionary compensation plan at issue was entirely fair to the stockholders and the corporation. To this end, the Delaware Supreme Court has narrowed this requirement in certain other cases involving interested transactions.[150]

One such type of case is where a controlling stockholder stands on both sides of a transaction, such as a buyout of the minority-owned stock.[151] In those cases, the Delaware Supreme Court has enabled the defendant(s) to shift the burden of persuasion to the plaintiffs entirely by obtaining either (i) an informed vote of a majority of the disinterested stockholders,[152] or (ii) approval of the transaction by an independent

[144] *See id.*

[145] *See* Orman v. Cullman, 794 A.2d 5, 20–22 n.36 (Del. Ch. 2002) (discussing the application of entire fairness).

[146] *Id.*

[147] *See supra* discussion in Section III.A.

[148] *Orman*, 794 A.2d at 20–22 n.36.

[149] *See* Ams. Mining Corp. v. Theriault, 51 A.3d 1213, 1239 (Del. 2012).

[150] *See* Kahn v. Lynch Comm'n Sys., Inc., 638 A.2d 1110, 1116 (Del. 1994).

[151] *Id.*

[152] Rosenblatt v. Getty Oil Co., 493 A.2d 929, 937 (Del. 1985) ("However, approval of a merger, as here, by an informed vote of a majority of the minority

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committee of directors who have bargaining power and can ensure the majority stockholder does not dictate the terms of the transaction.[153] If *both* processes are utilized, the defendants can shift the standard of review from entire fairness to business judgment.[154]

Indeed, director compensation cases were already subject to entire fairness, and the Delaware courts addressed the practical implications of those by shifting the standard of review to business judgment *if* the board of directors obtained stockholder approval.[155] At a minimum, stockholder ratification of plans in which directors retain discretion in awarding themselves compensation should continue to provide *some* value. The *Investors Bancorp* decision nullifies stockholder ratification as a tool to shift the burden to business judgment.[156] In the opinion, the Delaware Supreme Court did not address what role, if any, stockholder ratification will play in the future.[157] But it should serve some purpose.

In 2015, the Delaware Supreme Court recognized the value and policy rationale of stockholder ratification in a merger case, *Corwin v. KKR Financial Holdings LLC*.[158] In holding that stockholder ratification shifted the burden from enhanced scrutiny, Delaware corporate law's intermediate standard of review, to business judgment, the Delaware Supreme Court explained that it had been long-standing policy for the judiciary to refrain from second-guessing a decision by disinterested stockholders on the economic merits of a transaction.[159] The Delaware Supreme Court observed that when "disinterested equity owners–can easily protect themselves at the ballot box by simply voting

shareholders, while not a legal prerequisite, shifts the burden of proving the unfairness of the merger entirely to the plaintiffs.").

[153] Emerald Partners v. Berlin, 726 A.2d 1215, 1222 (Del. 1999) (identifying the use of a special committee to shift the burden of persuasion).

[154] *See, e.g.*, Kahn v. M & F Worldwide Corp., 88 A.3d 635, 644 (Del. 2014) ("We hold that business judgment is the standard of review that should govern mergers between a controlling stockholder and its corporate subsidiary, where the merger is conditioned *ab initio* upon both the approval of an independent, adequately-empowered Special Committee that fulfills its duty of care; and the uncoerced, informed vote of a majority of the minority stockholders.").

[155] *See In re* Inv'rs Bancorp, Inc. Stockholder Litig., 177 A.3d 1208, 1216–22 (Del. 2017) (discussing previous Delaware courts applying entire fairness for director compensation unless there was shareholder ratification and certain discretionary parameters).

[156] *See supra* notes 1–4 and accompanying text.

[157] *See In re Inv'rs Bancorp,* 177 A.3d at 1223 (stating that even after shareholder ratification, discretionary actions regarding director compensation must comport with fiduciary duties).

[158] *See* Corwin v. KKR Fin. Holdings LLC, 125 A.3d 304, 306, 308 (Del. 2015) (holding that the approval of the disinterested stockholders of a merger shifted the standard of review from enhanced scrutiny to business judgment).

[159] *Id.* at 312–13.

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no, the utility of litigation-intrusive standard of review promises more costs to stockholders in the form of litigation rents and inhibitions on risk-taking than it promises in terms of benefits to them."[160] Although the economic merits of a discretionary plan are not sufficiently clear to justify shifting the burden to the business judgment standard of review, which appears to be the Delaware Supreme Court's view,[161] stockholder ratification of such plans warrants inclusion in the determination of *on whom* the burden shall fall.

As Chancellor Allen observed in *Lewis*, a board of directors does not have to seek stockholder approval in order to compensate itself.[162] He explains four possible effects stockholder ratification can have on an interested transition.[163] The most useful in this scenario, as *Investors Bancorp* has nullified the one previously used, is that stockholder "ratification [can] shift[] the burden of unfairness to [the] plaintiff, [while] leav[ing in place the] shareholder-protective test."[164] That is, if stockholders ratify a discretionary compensation plan, rather than shifting the burden from entire fairness to business judgment, as it did in the past, such ratification would shift the burden of proving entire fairness from the director defendants to the stockholder plaintiffs.

This suggested use of stockholder ratification should appease the Delaware Supreme Court. In *Investors Bancorp*, the Delaware Supreme Court was concerned with foreclosing the possibility of equitable review on discretionary compensation.[165] The Delaware Supreme Court believed such transactions should be twice-tested: first for legal authorization, then by equity.[166] This proposed use of stockholder ratification does just that while balancing the practical implications of having such an exacting standard of review. Shifting the burden of persuasion leaves in place the "shareholder-protective test" but puts the onus on the challenging plaintiffs to prove that the putative compensation is unfair.[167] Should plaintiffs meet this burden, defendants will ultimately be required to prove that their compensation was entirely fair to the corporation.[168] Although not a comprehensive

[160] *Id.* at 313.

[161] *Id.* at 313–14.

[162] Lewis v. Vogelstein, 699 A.2d 327, 333–34 (Del. Ch. 1997) (explaining that the board can still compensate itself without seeking stockholder approval, but entire fairness will be the standard of review should a stockholder sue).

[163] *Id.* at 334.

[164] *Id.* (alteration in original).

[165] *In re* Inv'rs Bancorp, Inc. Stockholder Litig., 177 A.3d 1208, 1222–23 (Del. 2017).

[166] *Id.*

[167] *See Lewis*, 699 A.2d at 334.

[168] *In re Inv'rs Bancorp,* 177 A.3d at 1211.

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remedy, this Solomonic compromise somewhat mitigates the chances of costly strike suits, which inevitably harm stockholders, and at the same time maintains the "twice-tested" framework for the inherently interested transaction.

V. CONCLUSION

Investors Bancorp presented the Delaware Supreme Court with a challenging case. The dilemma confronted was an inherently interested transaction in which some corporations were taking advantage of stockholder ratification.[169] The court of chancery attempted numerous times to promulgate fixes in similar challenges and reconcile prior case law with the facts at hand.[170] Although it could have disposed of the case through different avenues, the Delaware Supreme Court refused.[171]

Discretionary compensation plans still offer a corporation the most efficient way to pay their current directors and entice new ones to join the board. The practical implications of entire fairness may harm a board of directors' ability to use this tool. If Delaware courts can still give some credence to stockholder ratification of discretionary plans, boards of directors, corporations, and their stockholders will be better off, because this will preserve both flexibility in a board's ability in compensating itself and the equitable review of such plans, while softening the practical limitations of entire fairness.

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[169] *Id.* at 1212–1216.
[170] *Id.* at 1222.
[171] *See id.* at 1211.