

August 16, 2019

## **DELAWARE COURT OF CHANCERY ISSUES IMPORTANT RULING ON VALIDITY OF ADVANCE NOTICE BYLAWS**

To Our Clients and Friends:

In an important transcript ruling issued this week,<sup>[1]</sup> the Delaware Court of Chancery upheld the validity and vitality of advance notice bylaw provisions, which govern the timing and disclosure requirements of stockholder nominations of board candidates. The ruling should give further comfort to boards of public corporations in enforcing reasonable and customary safeguards commonly imposed on the critical director nomination process.

The recent transcript ruling was issued in connection with the unsolicited efforts by Bay Financial Capital to acquire Barnes & Noble Education, Inc. (BNED). BNED operates physical and virtual bookstores for educational institutions, sells textbooks wholesale, and provides digital educational solutions. BNED was spun off from Barnes & Noble, Inc. in 2015. BNED's bylaws require that director nominations be submitted by stockholders no earlier than 120 days and no later than 90 days prior to the anniversary date of the prior year's annual meeting of stockholders. As customary, under BNED's bylaws a stockholder must be a record holder as of the notice deadline in order to nominate directors.

Between February and June 2019, Bay Capital submitted three unsolicited proposals to acquire BNED. The BNED Board rejected all three proposals, primarily for two reasons. First, the Board determined the financial consideration to be inadequate. Second, the Board believed that Bay Capital was not a credible potential acquirer, having doubts of its ability to finance an acquisition of a public company.

On June 27, 2019, the last day to submit director nominations for the 2019 annual meeting of stockholder, Bay Capital noticed the nomination of a slate of director candidates. Although the notice was timely, as of June 27 Bay Capital was just a beneficial owner of BNED stock and not a record holder. BNED's Board of Directors therefore rejected the notice as invalid. Two weeks later, Bay Capital filed a complaint in Delaware Court of Chancery seeking injunctive relief to run its slate of directors at the upcoming annual meeting of stockholders.

The Court found that despite being reminded no fewer than four times by its advisor of the record holder requirement set forth in the BNED bylaws, Bay Capital did not acquire shares until three days before the nomination deadline. And when the shares were acquired, it was done through a broker such that there was not sufficient time to get the shares transferred in Bay Capital's record name.

The Court dismissed various arguments advanced by Bay Capital in seeking an injunction, including a purported ambiguity in the BNED bylaws as to the need for the nominating stockholder to be a holder of record at the time it delivered the notice of nomination. Ultimately, the Court noted:

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“Needless to say, not even Delaware's strong public policy favoring the stockholder franchise will save Bay Capital from its dilatory conduct. Bay Capital blew the deadline. It then made up excuses for doing so. No record evidence suggests that the company is in any way at fault for that mistake. If this Court required the company to accept the nomination in these circumstances, advance notice requirements would have little meaning under Delaware law.”

In light of the continuing prevalence of shareholder activism and hostile takeover activity, public corporations should continuously review their advance notice bylaw with counsel to confirm that they include state-of-the-art guardrails that can ensure an orderly and timely nomination process. And, more importantly, well-informed boards should feel comfortable uniformly enforcing those provisions, and not be intimidated by efforts by activist shareholders and hostile bidders to try to bypass their requirements due to carelessness or ignorance.

Gibson Dunn represents Barnes & Noble Education, Inc. in this matter.

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[1] *Bay Capital Finance, LLC v. Barnes & Noble Education, Inc.* (August 14, 2019), available here.



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