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## Should You Consider Texas as Your Jurisdiction for a U. S. Corporation?

In the United States, companies can incorporate in any state of their choosing, regardless of where the company is headquartered or operates. The corporate law of the selected state will govern the internal affairs of the company, even if the company exists within that state only on paper.<sup>1</sup>

The State of Delaware has long been the domicile-of-choice for U.S. corporations publicly listed on a U.S. securities exchange.<sup>2</sup> Recently, some high profile corporations, such as Tesla, Inc. and Tripadvisor Inc., have changed or considered changing their state of incorporation from Delaware to Texas, Nevada, or another state, primarily based on the perception that Delaware courts are becoming less deferential to directors' decisions, particularly for corporations with controlling shareholders.<sup>3</sup> This article discusses key factors in considering Texas as a corporate domicile.<sup>4</sup>

### I. Introduction

Texas lawmakers and other constituencies have been intentionally developing Texas as an appealing corporate law jurisdiction, seeking to offer a sophisticated, predictable, and business-friendly legal environment.<sup>5</sup> A critical turning point in this effort occurred in 2003 with the reorganization of Texas business entity law from separate acts into the comprehensive Texas Business Organizations Code ("TBOC").<sup>6</sup> In 2023, Texas approved the creation of the Texas Business Court, allowing removal of the most significant business law cases into a specialized court with a judiciary appointed by the governor, similar to Delaware's Court of Chancery. The Texas Business Court has concurrent jurisdiction with the Texas District Courts over a specific list of business law cases, including certain kinds of derivative actions, certain commercial disputes that meet amount-in-controversy requirements, or certain cases in which a publicly traded company or a subsidiary is a party.<sup>7</sup> The newly-appointed 15th Court of Appeals has exclusive jurisdiction over appeals from the Texas Business Court. Some influential organizations are seeking amendments to the TBOC intended to enhance Texas's appeal to new or re-domiciling corporations.

### II. Discussion

#### 1. Overview of Corporate Governance Systems and Fiduciary Duties

Texas and Delaware are similar with respect to corporate governance systems and fiduciary law and the common law concepts in which they are rooted. For example, directors and officers are generally subject to the same fiduciary duties in both states, Texas and Delaware each generally review corporate decision-making under a deferential standard of review known as the business judgment rule, and both jurisdictions provide shareholders the opportunity to bring a lawsuit on behalf of the corporation to remedy harms to the corporation. Nevertheless, there are differences that can be important.

##### a. Fiduciary Duties of Corporate Managers

Generally, directors and officers (collectively referred to herein as "*corporate managers*") of a Texas corporation are held to substantially the same fiduciary duty standards as corporate managers of a Delaware corporation – the duties

of care and loyalty.<sup>8</sup> In Texas, like Delaware, the duty of care provides that directors must handle his or her corporate duties with the care that an ordinarily prudent person would under similar circumstances.<sup>9</sup>

The duty of loyalty described by Texas courts requires directors to act in good faith and not allow their personal interests to prevail over the interests of the corporation. This duty of loyalty generally prohibits directors from usurping corporate opportunities, engaging in self-dealing to the detriment of the corporation, or otherwise taking unfair advantage of the corporation to benefit themselves. Texas courts state that the exercise of this duty requires an extreme measure of honesty, selflessness and good faith.<sup>10</sup> Notably, the standard in Texas for approving transactions by directors with conflicts of interest (so called "*interested directors*") that may violate the duty of loyalty is very similar to that of Delaware, requiring disclosure of material facts and ratification of the

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1 This article addresses U.S. state law corporations. Limited liability companies and partnerships are generally very flexible and driven by freedom of contract principles in most, if not all, U.S. jurisdictions. Additionally, most state law differences are irrelevant for matters relating to wholly-owned subsidiaries.

2 As of 2023, 67.6 % of Fortune 500 companies were incorporated in Delaware, and 80 % of all U.S.-based initial public offerings in 2023 chose Delaware as their corporate home. See Delaware Division of Corporations: 2023 Annual Report (2023), <https://corpfiles.delaware.gov/Annual-Reports/Division-of-Corporations-2023-Annual-Report.pdf>.

3 See Kevin LaCroix, Delaware or Another State: What's the Difference?, The D&O Diary (6 May 2024), <https://www.dandodiary.com/2024/05/articles/corporate-law/delaware-or-another-state-whats-the-difference/>.

4 For purposes of uniformity, this article uses the term "shareholder" instead of "stockholder," with an exception for where the citation of caselaw or statutory provisions specifically uses the term "stockholder." The Texas Business Organizations Code ("TBOC") uses the term "shareholder" and the Delaware General Corporation Law ("DGCL") uses "stockholder." Additionally, for simplicity, we refer to both the certificate of formation (used in Texas) and the certificate of incorporation (used in Delaware) as the "charter." The TBOC may be found online at <https://statutes.capitol.texas.gov/Docs/SDocs/BUSINESSORGANIZATIONSCODE.pdf>, and the DGCL may be found online at <https://delcode.delaware.gov/title8/c001/>.

5 This article will focus on Texas corporate law, but the TBOC also governs the formation and operation of partnerships and limited liability companies.

6 The TBOC consolidated the provisions of statutes governing domestic for-profit corporations, nonprofit corporations, professional corporations, professional associations, limited partnerships, limited liability companies, partnerships, real estate investment trusts, cooperative associations, and unincorporated nonprofit associations. See Jane Nelson, Business Organizations Code FAQs, Texas Secretary of State (2024), <https://www.sos.state.tx.us/corp/bocfaqs.shtml>.

7 Tex. Gov't Code ("TGC") § 25A.004.

8 See *Gearhart Indus., Inc. v. Smith Int'l, Inc.*, 741 F.2d 707, 719-23 (5th Cir. 1984) (addressing Texas law); *Ritchie v. Rupe*, 443 S.W.3d 856, 868 (Tex. 2014); *Loy v. Harter*, 128 S.W.3d 397, 407 (Tex. App. – Texarkana 2004, pet. denied); *Gantler v. Stephens*, 965 A.2d 695, 708-09 (Del. 2009).

9 See *Gearhart*, 741 F.2d at 720 (addressing Texas law).

10 *Loy*, 128 S.W.3d at 407; *Int'l Bankers Life Ins. Co. v. Holloway*, 368 S.W.2d 567, 577 (Tex. 1963); *Landon v. S & H Mktg. Grp., Inc.*, 82 S.W.3d 666, 672-73 (Tex. App. – Eastland 2002, no pet.).

transaction by disinterested directors or shareholders.<sup>11</sup> However, as discussed in Section II.1.e, Texas statutes identify circumstances in which a director is deemed not to have a material financial interest in a transaction and, therefore, does not constitute an interested director.<sup>12</sup>

In both Texas and Delaware, the duty of loyalty may also be breached by a failure in oversight, when a board abdicates its responsibilities and fails to exercise any judgment.<sup>13</sup> Texas courts, similar to Delaware, also emphasize the duties of candor (*i.e.*, full disclosure to shareholders respecting matters that affect the principal's interests, such as a business opportunity) and confidentiality, both of which are drawn from the duty of loyalty.<sup>14</sup>

Unlike Delaware, Texas specifically enumerates a third fiduciary duty: the duty of obedience. This is characterized as the duty to follow the law, which prohibits a director of a Texas corporation from acting beyond the scope of the corporation's powers as defined by the corporation's charter and Texas law.<sup>15</sup> There is little case law in Texas addressing the duty of obedience, but it is similar in concept to Delaware's *ultra vires* doctrine (which allows a shareholder to bring suit against an incumbent or former officer or director who causes a corporation to exceed the specific corporate purpose set forth in the articles of incorporation)<sup>16</sup> and is consistent with Delaware caselaw ruling that "*Delaware law does not charter lawbreakers.*"<sup>17</sup>

#### b. To Whom are Fiduciary Duties Owed?

Under both Texas and Delaware law, directors have a duty to act in the best interest of the corporation and its shareholders as a group.<sup>18</sup> Texas does not generally recognize a fiduciary or common law claim for oppression of minority shareholders.<sup>19</sup> Instead, Texas has codified minority shareholder protections in Section 11.404 of the TBOC. Specifically, if a governing person of a Texas corporation engages in "*illegal, oppressive, or fraudulent*" conduct, a minority shareholder can petition the court to appoint a rehabilitative receiver to take over the corporation's governance.<sup>20</sup> To obtain this remedy, a minority shareholder must prove malice (intent to harm) on the part of the governing person and that the actions taken by the same created a serious risk of harm to the corporation.<sup>21</sup> This is a high standard, and generally Texas courts are restrained in granting such a strong equitable remedy.<sup>22</sup>

#### c. May a Board Consider Other Interests?

Whether the sole purpose of a corporation should be to maximize profit for shareholders is a hotly-debated topic in American corporate law.<sup>23</sup> The traditional view is that a board must only seek to maximize profit for shareholders. However, more recently, scholars, practitioners, and business leaders have argued that a corporation can, and should, consider other stakeholders, such as customers, employees, suppliers, and communities.<sup>24</sup>

Generally, Delaware continues (but not without debate) to be a shareholder primacy-driven state,<sup>25</sup> although a for-profit public benefit corporation can be formed under the DGCL.<sup>26</sup> In contrast, Texas statutorily permits directors to consider not only "*the long and short-term interests of the corporation and its shareholders,*" but "*any social purpose specified in the corporation's certificate of formation.*"<sup>27</sup> Additionally, the Texas statute clarifies that "[n]othing [...] prohibits or limits a director or officer of a corporation that does not have a social purpose specified as a purpose in the corporation's certificate of formation from considering, ap-

proving, or taking an action that promotes or has the effect of promoting a social, charitable, or environmental purpose."<sup>28</sup> Thus, Texas is more explicit in authorizing an ordinary corporation to consider an expanded range of constituencies.

#### d. Standards of Review for Breaches of Fiduciary Duties

Through its extensive case law, Delaware has established three standards of review to evaluate director decision-making: the business judgment rule, enhanced scrutiny, and entire fairness.<sup>29</sup>

The business judgment rule is the default standard of review and presumes that, in making a business decision, the directors of a corporation were disinterested and acted on an informed basis, in good faith, and in the honest belief that the action taken was in the best interests of the corporation.<sup>30</sup> When the business judgment rule applies, a decision of directors "*will be upheld unless it cannot be attributed to any rational purpose.*"<sup>31</sup>

Entire fairness, the most stringent standard of review, applies when there is a "*disabling conflict of interest*" and

11 DGCL § 144; TBOC § 21.418(b).

12 TBOC § 1.003.

13 *FDIC v. Harrington*, 844 F. Supp. 300, 306 (N.D. Tex. 1994); *see also In re Caremark Int'l Inc. Derivative Litig.*, 698 A.2d 959, 969-70 (Del. Ch. 1996).

14 *Icom Systems, Inc. v. Davies*, 990 S.W.2d 408, 410 (Tex. App. – Texarkana 1999, no pet.); *Int'l Bankers Life Ins. Co.*, 368 S.W.2d at 576-77; *Landon*, 82 S.W.3d at 672-73; *Arnold v. Soc'y for Sav. Bancorp, Inc.*, 650 A.2d 1270, 1280 (Del. 1994); *In re MONY Group S'holders Litig.*, 852 A.2d 9, 24-25 (Del. Ch. 2004); *Hollinger Int'l Inc. v. Black*, 844 A.2d 1022, 1062 (Del. Ch. 2004), *aff'd sub. nom.*, *Black v. Hollinger Int'l Inc.*, 872 A.2d 559 (Del. 2005); *Agranoff v. Miller*, C.A.No. 16795, 1999 WL 219650, at \*19 (Del. Ch. Apr. 12, 1999), *aff'd as modified*, 737 A.2d 530 (Del. 1999).

15 *Gearhart*, 741 F.2d at 719.

16 DGCL § 124.

17 *See In re Massey Energy Co.*, 2011 WL 2176479, at \*20 (Del. Ch. 2011).

18 *See Klaasen v. Allegro Dev. Corp.*, 2013 WL 5967028, at \*11 (Del. Ch. Nov. 7, 2013); *Ritchie*, 443 S.W.3d at 868-69, 874 n. 27; *Somers ex rel. EGL, Inc. v. Crane*, 295 S.W.3d 5, 11 (Tex. App. – Houston [1st Dist.] 2009, pet. denied); *Hoggett v. Brown*, 971 S.W.2d 472, 488 (Tex. App. – Houston [14th Dist.] 1997, pet. denied); *Gearhart*, 741 F.2d at 721-24; *Holloway*, 368 S.W.2d at 576-78.

19 *See Ritchie*, 443 S.W.3d at 877-91.

20 TBOC §§ 11.404(a)-(c).

21 *Ritchie*, 443 S.W.3d at 871.

22 *See Balias*, 748 S.W.2d at 257.

23 *See, e.g., Leo E. Strine, Jr.*, Making It Easier for Directors to "Do the Right Thing"?, 4 Harv. Bus. L. Rev. (2014), 235, 236 (collecting authorities).

24 For example, the Business Roundtable, an association of 200 CEOs of America's leading companies, issued a statement redefining their vision of the purpose of the corporation. Business Roundtable Redefines the Purpose of a Corporation to Promote 'An Economy That Serves All Americans', Business Roundtable (19 August 2019), <https://www.businessroundtable.org/business-roundtable-redefines-the-purpose-of-a-corporation-to-promote-an-economy-that-serves-all-americans>.

25 *See McRitchie v. Zuckerberg*, 315 A.3d 518, 536-579 (Del. Ch. 2024); *Leo E. Strine, Jr.*, The Dangers of Denial: The Need for a Clear-Eyed Understanding of the Power and Accountability Structure Established by the Delaware General Corporation Law, 50 Wake Forest L. Rev. (2015), 761. *But see id.* at n. 9 (collecting contrary authorities); *see also eBay Domestic Hldgs., Inc. v. Newmark*, 16 A.3d 1, 33 (Del. Ch. 2010) ("When director decisions are reviewed under the business judgment rule, this Court will not question rational judgments about how promoting non-stockholder interests [...] ultimately promote stockholder value.").

26 *See* DGCL § 361.

27 TBOC § 21.401.

28 *Id.* § 21.401(e).

29 *Reis v. Hazelett Strip-Casting Corp.*, 28 A.3d 442, 457 (Del. Ch. 2011).

30 *See Aronson v. Lewis*, 473 A.2d 805, 812 (Del. 1984); *see also Smith v. Van Gorkom*, 488 A.2d 858, 878, 880 (Del. 1985).

31 *Reis*, 28 A.3d at 457 (quoting *In re Walt Disney Co. Deriv. Litig.*, 906 A.2d 27, 74 (Del. 2006)).

requires the directors to prove the challenged transaction was entirely fair to the corporation and its shareholders.<sup>32</sup> For instance, controlling shareholders of a Delaware corporation who receive a material non-ratable benefit that is not shared with all shareholders must satisfy the entire fairness standard of review.<sup>33</sup> If entire fairness applies to a challenged transaction, the directors must show the transaction was the product of both fair price and fair dealing.<sup>34</sup> “Not even an honest belief that the transaction was entirely fair will be sufficient to establish entire fairness. Rather, the transaction itself must be objectively fair, independent of the board’s beliefs.”<sup>35</sup>

Enhanced scrutiny applies a “reasonableness” test to assess director action and sits between the deferential business judgment rule and the exacting entire fairness standard. It applies “when a board adopts defensive measures to protect against a hostile takeover” or in the context of a change of control transaction.<sup>36</sup> Two seminal Delaware cases, *Unocal v. Mesa Petroleum Co.* and *Revlon, Inc. v. MacAndrews & Forbes Holdings, Inc.*, set forth these two variants of enhanced scrutiny.<sup>37</sup> Under *Unocal*, target boards who adopt deal protection measures must show (1) they “had reasonable grounds for believing that a danger to corporate policy and effectiveness existed” and (2) any measure taken was “reasonable in relation to the threat.”<sup>38</sup> *Revlon* duties require directors to take steps reasonably designed under the applicable circumstances to get the best price reasonably available once a corporation is put up for sale.<sup>39</sup> Recently, the Delaware Court of Chancery held that enhanced scrutiny also applies to controlling shareholders when they have “subtle” conflicts of interest and have taken action in areas traditionally reserved for the board of directors.<sup>40</sup>

Notably, Delaware allows for business judgment rule deference to be restored in cases where higher standards of scrutiny would apply if certain procedural protections are met.<sup>41</sup>

To date, Texas has not formally adopted enhanced scrutiny or entire fairness as elevated standards of review, and for Texas corporations the business judgment rule is the standard of review of a director’s corporate decision making.<sup>42</sup> Because of this, corporate managers may have more freedom under Texas case law to implement defensive measures or facilitate transactions, including a transaction with a controlling shareholder.

#### e. Standard for Qualifying as a Disinterested Director

Conflicted-board and interested director transactions are an often-litigated area of corporate law, and both Texas and Delaware generally require approval by “disinterested” directors. The circumstances in which a director of a Texas corporation will be treated as per se “disinterested” appear to be broader than in Delaware. Directors are disinterested under Texas statute as long as they (i) are not a party to the contract or transaction, (ii) are not materially involved in the conduct that is subject to challenge, and (iii) do not have a material financial interest in the outcome of the contract or transaction.<sup>43</sup>

The Texas statute explicitly enumerates categories that, if applicable, do not by themselves result in a director having a material financial interest, including: (1) the person was nominated or elected as a governing person by someone who has an interest in the matter or is alleged to have an interest; (2) the person receives normal fees or customary compensation, reimbursement for expenses, or benefits as a governing person of the corporation; (3) the person has a direct or indirect equity interest in the entity; (4) the entity or its

subsidiaries have an interest in the matter or are affected by the alleged conduct; (5) the person receives ordinary and reasonable compensation for reviewing and making recommendations on the disposition of the issue at hand; or (6) the person either (A) is named in the case as a defendant or (B) voted to approve or acquiesced to the act being challenged.<sup>44</sup> While a number of these may also not result in a material interest under Delaware law, the Texas statute provides helpful clarification.

#### f. Derivative Litigation and Rights

When corporate managers breach their fiduciary duties to the corporation, individual shareholders may bring a lawsuit on behalf of the corporation in order to remedy the harm suffered by the corporation. This type of lawsuit is called a “derivative” lawsuit.

Texas limits derivative litigation by requiring a written demand on the corporation (even if demand is believed to be futile) and imposing a 90-day waiting period before the suit can be initiated.<sup>45</sup> However, the 90-day waiting period is not required if the corporation has notified the shareholder that the corporation has rejected the demand, the corporation is suffering irreparable injury, or irreparable injury would result if the shareholder waited 90 days.<sup>46</sup>

To have standing in Texas for a derivative claim, a shareholder (1) must have been a shareholder at the time of the alleged act or omission or have acquired his or her shares by operation of law from someone who was a shareholder at that time and (2) must fairly and adequately represent the interests of the corporation in enforcing the rights of the corporation.<sup>47</sup> Statutorily, Delaware only requires element one.<sup>48</sup>

Once a derivative claim is initiated, a Texas corporation must determine how to proceed by an affirmative vote of the

32 *Amir N. Licht*, Farewell to Fairness: Towards Retiring Delaware’s Entire Fairness Review, 44 Del. J. Corp. L. 1(2020), 5-6; *In re Trados Inc. S’holder Litig.*, 73 A.3d 17, 44 (Del. Ch. 2013) (“Entire fairness, Delaware’s most onerous standard, applies when the board labors under actual conflicts of interest.”).

33 *See Maffei v. Palkon*, No. 125-2024, 2025 WL 384054, at \*17-19 (Del. Feb. 4, 2025); *Weinberger v. UOP*, 457 A.2d 701, 711 (Del. 1983); *see also In re Sears Hometown & Outlet Stores, Inc. S’holder Litig.*, 309 A.3d 474, 514 (Del. Ch.), modified on reargument, (Del. Ch. 2024).

34 *See Weinberger*, 457 A.2d at 711; *see also In re Sears, Inc. S’holder Litig.*, 309 A.3d at 514.

35 *Reis*, 28 A.3d at 459.

36 *Jhonattan Gonzalez*, *Corwin Cleansing: A Doctrine Well Established in Delaware Jurisprudence*, 15 Rutgers Bus. L. R. (2020), 250, 252; *see In re Trados Inc. S’holder Litig.*, 73 A.3d at 44.

37 *Unocal Corp. v. Mesa Petroleum Co.*, 493 A.2d 946, 955 (Del. 1985); *Revlon, Inc. v. MacAndrews & Forbes Holdings, Inc.*, 506 A.2d 173, 182 (Del. 1986).

38 *Unocal*, 493 A.2d at 955.

39 *Revlon*, 506 A.2d at 182.

40 *In re Sears, Inc. S’holder Litig.*, 309 A.3d at 583-85, 512-19.

41 *See Corwin v. KKR Fin. Holdings LLC*, 125 A.3d 304, 305-14 (Del. 2015) (holding that the business judgment rule applies if the challenged transaction is not subject to entire fairness and is approved by a majority of disinterested, fully informed stockholders); *Kahn v. M & F Worldwide Corporation*, 88 A.3d 635, 644 (Del. 2014) (applying business judgment deference, as opposed to entire fairness, to a conflicted controller merger where the merger was conditioned upon the approval of an independent, adequately-empowered special committee and the uncoerced, informed vote of a majority of the minority stockholders).

42 *See Gearhart*, 741 F.2d at 719-25.

43 TBOC § 1.003(a).

44 *Id.* § 1.003(b).

45 *Id.* § 21.553(a).

46 *Id.* § 21.553(b).

47 *Id.* § 21.552.

48 DGCL § 327.



majority of (1) all independent and disinterested directors of the corporation;<sup>49</sup> (2) a committee of one or more independent and disinterested directors appointed by an affirmative vote of the majority of one or more independent and disinterested directors; or (3) a panel of one or more independent and disinterested individuals appointed by the court on a motion by the corporation.<sup>50</sup> The court may stay a derivative action for not more than 60 days (which may be continued under certain circumstances) to allow the board or independent persons to evaluate the claim.<sup>51</sup> A Texas plaintiff has limited discovery rights and can only challenge the lack of independence or disinterest, good faith, or reasonable procedures of the disinterested and independent persons conducting the review.<sup>52</sup> Finally, under Texas law, court approval is not required for the discontinuance or settlement of a derivative proceeding unless the court determines that a discontinuance or settlement substantially affects the interests of other shareholders.<sup>53</sup>

In contrast, under Chancery Court Rule 23.1 – the rule governing Delaware derivative litigation – plaintiff shareholders do not need to make a “demand” on the board if they can plead particularized facts that show such demand would be futile (*i.e.*, that the directors upon whom the demand would be made are incapable of making an impartial decision regarding the demand or the challenged transaction was not the product of a business judgment).<sup>54</sup> Similarly, Rule 23.1 states that a derivative action may be dismissed or settled only with court approval to ensure that the resolution is fair and reasonable to the corporation and its shareholders. Moreover, shareholders must be notified of any proposed settlement or dismissal, allowing them an opportunity to object if they believe the terms are not in the corporation’s best interest.

## 2. Comparison of Codified Shareholder Rights

While much of the focus of the prior discussion of Texas versus Delaware has been on the case law and courts, the TBOC and DGCL have other meaningful differences. At a high level, the TBOC and DGCL provide similar statutory rights and protections to shareholders. However, there are some distinctions between the two statutory regimes that could be important for companies choosing to domicile in Texas.

### a. Special Meetings and Written Consents

Delaware does not provide a mandatory statutory right for shareholders to call a special meeting of shareholders (but does allow such a right – which can be limited – to be included in the charter or bylaws).<sup>55</sup> Thus, by default, shareholders may only express their preferences through a shareholder vote at annual shareholder meetings and at special shareholder meetings called by the company’s board or management.

In contrast, in Texas, the holders of ten percent or more of all of the shares of a corporation entitled to vote at a proposed special meeting have the statutory right to call a special meeting unless the corporate charter requires a higher ownership percentage (which may not exceed 50 %).<sup>56</sup> Texas shareholders are guaranteed the special meeting right that Delaware shareholders lack.

There is no stated statutory restriction on the proposals that may be voted on at a special meeting called by shareholders of a Texas corporation,<sup>57</sup> and there is no case law addressing whether this might be limited through the charter or validly adopted bylaws.

Additionally, in Delaware, unless the corporate charter provides otherwise, shareholders may act by written consent of a majority.<sup>58</sup> Some Delaware corporations eliminate entirely the shareholder right to act by written consent by including a provision to that effect in the charter. In those circumstances, restoring the shareholder written consent right requires a charter amendment, which often requires the affirmative vote of the majority (or supermajority, depending on the charter) of the outstanding common stock.

The TBOC, in contrast, grants shareholders of Texas corporations the right to act by unanimous written consent, and the charter may authorize action through a written consent with less than unanimous approval if the consent is signed by shareholders holding the minimum number of votes necessary to take the action that is the subject of the consent.<sup>59</sup>

### b. Voting Rights

Many public corporations may establish more than one class or series of stock at an initial public offering in order to provide for a high-vote class of stock held by the founders and a publicly traded class of stock with one vote per share (or with no vote).<sup>60</sup> Classes of preferred stock may also be established with limited or no stated voting rights. The goals of these structures may include keeping voting power in the hands of the company’s founders, protecting a newer company from hostile M&A or activism, or facilitating financing transactions in which the investor requires a preferred return. Regardless of what the charter or certificate of designation for preferred stock state to be the voting rights of limited- or non-voting stock, both the TBOC and DGCL provide minimum voting rights to such classes of stock. Delaware practitioners generally advise that a corporation can expressly opt out of the minimum voting rights set forth in DGCL Section 242(b)(2), but a Texas corporation cannot opt out of the statutory minimum voting rights of the TBOC.

### aa. Charter Amendments

The charter is the key governing document of the rights of shareholders in a corporation and, in most cases, requires a shareholder vote to be amended. A majority vote of the outstanding stock entitled to vote is required to amend a charter in Delaware.<sup>61</sup> Unless otherwise entitled to vote in specific charter provisions, a separate class of shares is allowed to vote only if the proposed amendment: (1) increases or decreases the aggregate number of authorized shares of such class, (2) increases or decreases the par value of the shares of

49 It is possible for a “disinterested” director not to be “independent” under Texas law. The independence for a director of a Texas corporation is measured by the standards set forth in TBOC § 1.004, whereas the status of such person as “disinterested” is measured by standards set forth in the immediately preceding TBOC § 1.003.

50 TBOC § 21.554.

51 *Id.* § 21.555.

52 *Id.* §§ 21.556, 21.558(b).

53 *Id.* §§ 21.560(a)-(b).

54 See *Brehm v. Eisner*, 746 A.2d 244, 256 (Del. 2000); *Litt v. Wycoff*, 2003 WL 1794724, at \*6 (Del. Ch. 28 March 2003).

55 DGCL § 211(d).

56 TBOC § 21.352(a)(2).

57 See *id.* § 21.352(c) (limiting business to that described in the notice); *id.* § 21.353 (lacking limits on purpose of the meeting).

58 DGCL § 228(b).

59 TBOC §§ 6.201-02.

60 For example, hundreds of public companies of all sizes have dual-class voting structures including AirBNB, Inc. (NASDAQ: ABBN), Alphabet, Inc. (NASDAQ: GOOG), Ford Motor Company (NYSE: F), Meta Platforms, Inc. (NASDAQ: META), The New York Times Company (NYSE: NYT), Tripadvisor, Inc. (NASDAQ: TRIP).

61 DGCL § 242(b)(1).

such class, or (3) alters or changes the powers, preferences, or special rights of the shares of such class so as to affect them adversely.<sup>62</sup> These voting rights apply even if the class of stock is designated as non-voting, unless the charter expressly rejects the provisions.<sup>63</sup>

In Texas, by contrast, “fundamental” actions,<sup>64</sup> including amending the corporate charter, require the “affirmative vote of the holders of at least two-thirds the outstanding shares entitled to vote on the fundamental action.”<sup>65</sup> When a class or series of shares is entitled to vote on a fundamental action, the action must be approved by at least two-thirds of the holders of shares in each class or series that was entitled to vote. In each case, the two-thirds vote shareholder may be reduced, but not below a majority, in the charter.<sup>66</sup>

The TBOC also specifies instances where separate voting by a class or series of shares is required for approval of a charter amendment, **even if that class or series does not expressly have voting rights in the charter**, including the following actions that would have an effect on the specified class or series (the “*affected shares*”): (i) increasing or decreasing the authorized number of affected shares; (ii) changing the par value of the affected shares; (iii) creating a new class or series of shares with rights equal or superior to the affected shares; (iv) enhancing the rights of another class or series relative to the affected shares; or (v) exchanging, reclassifying or cancelling all or part of the affected shares.<sup>67</sup>

In this way, Texas law grants separate classes of stock a veto right on certain charter amendments that may be unexpected for those accustomed to Delaware law and practice.

#### bb. Fundamental Business Transactions

In Delaware, approval of mergers, conversion, or transactions involving the sale of all or substantially all of a corporation’s assets requires a majority vote of all shareholders with a right to vote.<sup>68</sup> Delaware law does not mandate voting by different classes or series of shares, except as set forth in Section II.2.b.i with respect to charter amendments.

In Texas, a corporation cannot undertake a fundamental business transaction<sup>69</sup> without shareholder approval. The TBOC establishes a default approval threshold of at least two-thirds of the outstanding shares of the corporation entitled to vote, but the charter can reduce the threshold to a majority vote.<sup>70</sup>

The TBOC features an important difference with respect to class voting in the context of a merger or “*fundamental business transaction*.” Texas shareholders, including classes or series of preferred shareholders, are given a class or series vote on fundamental business transactions if the class or series of shares will be “*converted into or exchanged for other securities, interests, obligations, rights to acquire shares, interests, or other securities, cash, property, or any combination*” of those categories.<sup>71</sup> However, separate voting by a class or series of shares of a corporation is not required for approval of a sale of all or substantially all of the assets of a corporation unless that class or series is given that right in the corporation’s charter.<sup>72</sup>

#### cc. Anti-Takeover Statutes

Both Delaware and Texas have antitakeover statutes that provide that if an interested shareholder acquires shares of voting common stock over a certain threshold without prior approval of the target’s board, then the interested shareholder may not engage in a business combination with the target for a period of three years unless a supermajority of

the target’s shareholders approve the transaction. Delaware sets the percentage threshold at 15 % ownership, while Texas requires 20 % ownership of the outstanding voting shares.<sup>73</sup>

Delaware also has an exception to allow transactions that resulted in the shareholder becoming an interested shareholder if “*the interested shareholder owned at least 85 % of the voting stock of the corporation outstanding at the time the transaction commenced*.”<sup>74</sup> Both Texas and Delaware allow corporations to opt out of this requirement in their charters.<sup>75</sup>

#### c. Information and Inspection Rights

Shareholder information and inspections rights are valuable to shareholders as tools to keep a check on bad management. However, shareholders who lack a bona fide purpose in invoking such rights can cause undue expense and burden on the corporation.

In Texas, qualified shareholders who have held the company’s shares for at least six months immediately preceding the shareholder’s demand to inspect or hold at least five percent of all the outstanding shares have the right to examine and copy the relevant books and records for any proper purpose at any reasonable time.<sup>76</sup> Caselaw interpreting “*proper purpose*” is limited, but an improper purpose is a defense to a books-and-records request.<sup>77</sup> The party invoking the defense must prove that the shareholder is not seeking the information to protect the corporation or the shareholders, but instead is “*actuated by corrupt or unlawful motives*.”<sup>78</sup>

Unlike Texas, Delaware does not condition shareholder information and inspection rights on duration of share ownership or amount of share ownership. Accordingly, Delaware shareholders may inspect and copy the corporation’s stock ledger, a list of its shareholders, and other books and records for any proper purpose.<sup>79</sup> Delaware caselaw regarding these topics, and what constitutes a “*proper purpose*,” is extensive.

<sup>62</sup> *Id.* § 242(b)(2).

<sup>63</sup> *Id.*

<sup>64</sup> Fundamental actions include “(1) an amendment of a certificate of formation, including an amendment required for cancellation of an event requiring winding up in accordance with Section 11.152(b); (2) a voluntary winding up under Chapter 11; (3) a revocation of a voluntary decision to wind up under Section 11.151; (4) a cancellation of an event requiring winding up under Section 11.152(a); or (5) a reinstatement under Section 11.202.” TBOC §§ 21.364(a)(1)-(5).

<sup>65</sup> *Id.* § 21.364(b).

<sup>66</sup> *Id.* §§ 21.364(b), 21.365. Exceptions are so limited that they are not worth mentioning in this article.

<sup>67</sup> *Id.* § 21.364(d) lists thirteen different charter amendment impacts that require a separate class or series vote; five have been listed above.

<sup>68</sup> See DGCL §§ 251(c), 266(b), 271(a).

<sup>69</sup> Fundamental business transactions includes mergers, interest exchanges, conversions, and sales of all or substantially all of a corporation’s assets. TBOC § 1.002(32).

<sup>70</sup> *Id.* § 21.365.

<sup>71</sup> *Id.* § 21.458(a)(1).

<sup>72</sup> *Id.* § 21.458(c).

<sup>73</sup> TBOC § 21.602(a)(1); DGCL § 203(c)(5).

<sup>74</sup> DGCL § 203(a)(2).

<sup>75</sup> See DGCL § 203(b)(1); TBOC § 21.607(1)(A).

<sup>76</sup> TBOC §§ 21.201(b), 21.218.

<sup>77</sup> See *id.* § 21.222(b)(4).

<sup>78</sup> *Third Eye, Inc. v. UST Glob. Inc.*, No. 05-22-00334-CV, 2023 WL 3243482, at \*3 (Tex. App. – Dallas 2023), review denied (Oct. 6, 2023) (quoting *Moore v. Rock Creek Oil Corp.*, 59 S.W.2d 815, 818 (Tex. 1933)).

<sup>79</sup> DGCL § 220(b).

#### d. Shareholder Appraisal Rights

Both Texas and Delaware allow appraisal rights for dissenting shareholders in certain situations, which are rights to have an independent valuation of a shareholder's shares by a court with respect to a proposed transaction.<sup>80</sup> In Texas, dissenting shareholders can seek appraisal rights in a merger, a sale of all or substantially all of the assets of a corporation, a plan of exchange, a plan of conversion, and a short-form merger.<sup>81</sup>

In Delaware, dissenting shareholders who own shares of a corporation involved in a merger, consolidation, conversion, transfer, domestication, or continuance have appraisal rights and can petition for a court to determine the fair value of their shares.<sup>82</sup> One key distinction here is that Texas allows appraisal rights when there is a sale of all or substantially all of the corporation's assets, while Delaware does not. Both states provide appraisal rights to minority holders in short-form mergers if their interests are exchanged or converted.<sup>83</sup>

Both Texas and Delaware have a market out exception.<sup>84</sup> The exception is similar in both states and does not allow appraisal rights for shares "listed on a national securities exchange" or for shares that are "held of record by more than 2,000 holders" in Delaware or "held of record by at least 2,000 owners" in Texas.<sup>85</sup> However, appraisal rights apply when shareholders are required to accept as consideration for their shares anything other than: (1) interests in the surviving corporation (listed on national security exchange or held of record by more than, or at least, 2,000 owners), (2) cash in lieu of fractional ownership interests, or (3) any combination of shares or fractional shares that fall under the previous requirements.<sup>86</sup> In short, where merger consideration includes cash (beyond that to compensate for fractional shares), Delaware shareholders are entitled to appraisal rights.

Finally, Delaware has a *de-minimis* standard applicable to appraisals; Texas does not.<sup>87</sup> The Delaware courts will dismiss an appraisal proceeding for a shareholder who was entitled to appraisal rights concerning shares listed on a national security exchange unless at least one of the following are met: "(1) the total number of shares entitled to appraisal exceeds 1 % of the outstanding shares of the class or series eligible for appraisal, (2) the value of the consideration provided in the merger [...] for such total number of shares exceeds \$1 million, or (3) the merger was approved [as a short-form merger]."<sup>88</sup>

#### 3. Standard of Conduct for Removal of Directors

Generally, directors serve until the end of their appointed term or until their death, resignation or removal from office. From time to time, shareholders may decide that a director should be removed before the end of his or her appointed term, which requires a shareholder vote under both Delaware and Texas law.

In Delaware, the default rule under the DGCL is that directors may be removed "*with or without cause*" by the holders of a majority of the shares then entitled to vote at an election of directors.<sup>89</sup> Companies with special board structures are given exceptions – when the board is classified, removal can be limited to "*for cause*" only, and corporations with cumulative voting also have special removal limitations.<sup>90</sup>

Texas, in contrast, offers a corporation the choice to provide a stronger protection to corporate directors. The TBOC default standard is that, in the absence of a charter or bylaw provision to the contrary, directors may be removed with or

without cause; nevertheless, the TBOC also states that "*a director of a corporation may be removed from office under any procedure provided by the certificate of formation or bylaws of the corporation.*"<sup>91</sup> Thus, a Texas corporation may adopt "*for cause only*" removal provisions in its charter or bylaws and limit director removal to cases where there is some sort of director misconduct.<sup>92</sup>

#### 4. Director Liability for Dividends

Texas and Delaware impose personal liability on directors who allow distributions (including share purchases) in violation of the applicable statutes.<sup>93</sup> The TBOC and DGCL both prohibit dividends that (i) violate the corporate charter or (ii) result in insolvency. In Texas, to declare a distribution a Board must also find that the amount distributed would not exceed the corporation's current distribution limit by utilizing financial statements and other information of the corporation as indicators.<sup>94</sup> In Delaware, a Board can declare a dividend from the corporation's surplus.<sup>95</sup> If there is no surplus, then the corporation may pay a dividend out of its net profits from the year which the dividend is declared and/or the preceding fiscal year.<sup>96</sup>

The TBOC provides that directors who vote for an unlawful distribution are personally liable for all or part of the excess amount unless that amount would have been permitted after the date the director authorized the distribution.<sup>97</sup> However, in Texas, a director is not jointly and severally liable to the corporation for the excess if the director, acting in good faith and with ordinary care, relies on statements, valuations, or information prepared by parties associated with the corporation in considering the assets to be valued.<sup>98</sup> Similarly, in Delaware a director is protected if relying in good faith on the records of the corporation and other information, reasonably believed to be based on an officer's, employee's, or other person's professional or expert knowledge.<sup>99</sup>

The TBOC is the exclusive basis of liability for a director's authorization of an unlawful distribution, nullifying other claims such as breach of fiduciary duty to creditors and tortious violations under the Uniform Fraudulent Transfer Act. There is not a similar nullifying provision in Delaware.<sup>100</sup> Both jurisdictions similarly find that a director liable for an improper distribution is entitled to contribution from other directors who are also liable for the distribution.<sup>101</sup> Under the TBOC, a liable director may also receive

80 See DGCL § 262; TBOC §§ 10.354, 21.460.

81 TBOC § 10.354(a).

82 DGCL § 262(b).

83 TBOC § 10.354(a)(1)(E); DGCL § 262(b)(3).

84 TBOC § 10.354(b); DGCL §§ 262(b)(1)-(2).

85 TBOC §§ 10.354(b)(1)(A)(i)-(ii); DGCL § 262(b)(1).

86 See TBOC § 10.354(b)(3); DGCL § 262(b)(2).

87 See DGCL § 262(g).

88 *Id.*

89 DGCL § 141(k).

90 *Id.*; see also *In re VAALCO Energy, Inc. Stockholder Litigation*, C.A. No. 11775-VCL (Del. Ch. Dec. 21, 2015) (TRANSCRIPT); *Rohe v. Reliance Training Network, Inc.*, 2000 WL 1038190 (Del. Ch. July 21, 2000).

91 TBOC § 22.211(a).

92 See *id.*

93 TBOC § 21.316; DGCL § 174(a).

94 TBOC § 21.303; § 21.314-15.

95 DGCL § 170(a). Surplus is defined at DGCL § 154 as "the excess of the net assets of the corporation over the aggregate par value of its capital stock."

96 DGCL § 170.

97 TBOC § 21.316(b).

98 TBOC §§ 21.316(a)-(c).

99 DGCL § 172.

100 TBOC § 21.316(d).



direct contribution from shareholders who knowingly accepted the unpermitted distribution, while under the DGCL directors (i) are subrogated against shareholders who knowingly accepted the unpermitted distribution and (ii) can indirectly assert the corporation's claim against the shareholders.

Liability in Texas for an unlawful distribution extends to two years after payment, as opposed to six years in Delaware, applying to all directors that voted for or assented to the distribution.<sup>102</sup> In Delaware, a negligence standard of liability applies to all directors except those who are absent or expressly dissent.<sup>103</sup>

## 5. Protection from Fiduciary Liability for Corporate Managers

Both Texas and Delaware allow corporations to protect directors against liability for certain breaches of fiduciary duties with provisions allowing the adoption of exculpation and indemnification provisions, and in the case of indemnification, certain mandatory provisions.

### a. Statutory Exculpation from Damages

Texas generally permits elimination of liability for duty of care violations by directors.<sup>104</sup> A corporation may eliminate the liability of a director for monetary damages to the corporation or shareholders for breaches of the duty of care in its charter except where the behavior involves: (1) breach of the person's duty of loyalty, (2) an act or omission not in good faith which constitutes a breach of duty to the corporation or involves intentional misconduct or a knowing violation of law, (3) a transaction from which the person received an improper benefit, or (4) an act or omission for which liability is expressly provided by an applicable statute.<sup>105</sup>

Delaware allows corporations to include provisions in their charters that exculpate both directors and officers from personal liability for monetary damages for breaches of fiduciary duty, except for breaches of loyalty, acts or omissions not in good faith, intentional misconduct, or knowing violations of law.<sup>106</sup> To date, Texas has not expanded exculpation to apply to officers.

### b. Indemnification and Advancement

Texas and Delaware are generally very similar with respect to the circumstances in which corporate managers must or may be indemnified. While there are differences in some articulated standards, it is unclear whether these result in material differences in practice.

#### aa. Mandatory and Permissive Indemnification

Corporations in both Texas and Delaware are required to indemnify current and former directors for reasonable expenses if the person is (i) named as a defendant due to a person's position and (ii) successful in defending the action.<sup>107</sup> A potential distinction is that Delaware requires mandatory indemnification "to the extent" the corporate manager was successful, as compared to Texas' requirement to indemnify only when a corporate manager is "wholly successful."<sup>108</sup>

Both Texas and Delaware permit indemnification beyond the mandatory requirement. In Texas, the corporate manager must have acted in good faith and in a manner reasonably believed to be in the corporation's best interests, while Delaware allows corporate managers to be indemnified as long as they reasonably believed actions not to be opposed to the corporation's best interests.<sup>109</sup>

### bb. Derivative Liability Indemnification

Texas limits permissive indemnification to reasonable expenses (and does not allow indemnification for a judgment, penalty, or fine) where a director is found liable to the corporation or found to have improperly received a personal benefit.<sup>110</sup> Courts are not allowed to order indemnification for anything beyond reasonable expenses if a director has been found liable to the corporation or found to have improperly received a personal benefit.<sup>111</sup> No indemnification is available for a director who is found liable for willful or intentional misconduct in performance of the director's duty to the corporation, breach of the director's duty of loyalty, or an act or omission not committed in good faith that constitutes a breach of duty owed to the corporation.<sup>112</sup>

Delaware allows indemnification where a director is found liable to the corporation but "only to the extent that the [court] determine[s] [...] that, despite the adjudication of liability but in view of all the circumstances of the case, such person is fairly and reasonably entitled to indemnity for such expenses which the [court] shall deem proper."<sup>113</sup>

### cc. Advancement of Expenses

Both Texas and Delaware allow for the advancement of expenses to current directors upon receipt of an undertaking to repay if the person is not entitled to be indemnified.<sup>114</sup> Texas has one additional requirement that the person seeking advancement must provide a written affirmation of the "person's good faith belief that the person has met the standard of conduct necessary for indemnification."<sup>115</sup>

### dd. Opting-Out Indemnification

Texas allows a corporation to "restrict the circumstances under which the enterprise must or may indemnify or may advance expenses to a person."<sup>116</sup> Delaware does not have similar language.

## 6. Judiciary and Other State Functions

Delaware's dominance in corporate litigation stems in large part from its extensive legal precedents and expert judiciary.<sup>117</sup> Chancellors are appointed to 12-year terms on the Delaware Court of Chancery, affording them significant judicial independence.<sup>118</sup> Other key features include a lack of juries, rapid decisions, and the fact that appeals from final judgments from the Chancery Court are automatic and go directly to the Delaware Supreme Court.

101 TBOC § 21.318(a); DGCL § 174(b).

102 TBOC § 21.317.

103 DGCL § 174.

104 *Id.* § 7.001.

105 *Id.*

106 DGCL § 102(b)(7).

107 See DGCL § 145; TBOC § 8.051.

108 DGCL § 145(c)(1); TBOC § 8.051(a).

109 TBOC § 8.101(a)(1)(B)(i); DGCL § 145(a).

110 TBOC § 8.102(b)(1).

111 *Id.* § 8.052.

112 *Id.* § 8.102(b)(3).

113 DGCL § 145(b).

114 DGCL § 145(e); TBOC § 8.104.

115 TBOC § 8.104(a)(1).

116 *Id.* § 8.003.

117 See Bernard S. Black, Is Corporate Law Trivial?: A Political and Economic Analysis, 84 Nw. U. L. Rev. (1990), 542, 589-90.

118 Del. Const. art. IV, § 3; see also Shane Goodwin, Texas vs. Delaware: Which State Will Shape the Future of Corporate Law?, The Columbia Law School Blue Sky Blog, (15 January 2025), <https://clsbluesky.law.columbia.edu/2025/01/15/texas-vs-delaware-which-state-will-shape-the-future-of-corporate-law/>.

In a significant milestone, on 1 September 2024, the Texas Business Court – a new specialized court system tailored to corporate and commercial litigation – began hearing business law cases.

These courts focus on commercial disputes involving corporate governance, derivative litigation, securities, fiduciary duties, and other complex commercial or business law matters. Jurisdictionally, the Texas Business Court may handle cases where the monetary threshold exceeds \$5 million or \$10 million, depending on the nature of the dispute (and including an exception for certain cases involving publicly traded companies),<sup>119</sup> which is intended to focus the courts on addressing significant corporate controversies. Judges must have at least ten years of experience in complex commercial litigation or transactional law<sup>120</sup> and are appointed by the Texas governor for two-year terms.<sup>121</sup> The short two-year term (as compared to Delaware's 12-year terms) has prompted questions about the continuity and predictability of the Texas Business Court.<sup>122</sup>

The Texas Business Court incorporates several procedural features designed to streamline litigation, including enhanced pleading requirements, mandatory written opinions on dispositive motions, and tolling of statutes of limitations for cases dismissed due to jurisdictional issues.<sup>123</sup> Additionally, unlike many general courts, the Business Court does not permit remote appearances for jury trials, emphasizing a more traditional courtroom environment. Filing fees are significantly higher than in district courts, reflecting the complexity and high-value nature of these cases. Appeals bypass geographically organized intermediate courts and are direc-

ted to the newly created 15th Court of Appeals, a body designed specifically to handle cases arising from the Business Court.<sup>124</sup> From the 15th Court of Appeals, cases may be further appealed to the Texas Supreme Court. Notably, unlike the Delaware Chancery Court, the Texas Business Court permits trying complex commercial disputes to a jury.<sup>125</sup>

The success of the new Texas Business Court will depend, in large part, on the Courts' ability to build a body of case law that provides clarity and predictability for litigants. Notably, Texas does not have a direct equivalent to the 12(b)(6) dismissal standard that exists in Delaware (and in federal courts). As a result, it can be more difficult to get a meritless lawsuit dismissed at the outset of litigation in Texas than in Delaware.

### III. Conclusion

In conclusion, Texas has a thoughtfully considered and detailed corporate statute. Some facets of the statute – such as meeting and voting rights – are arguably more favorable to shareholders than their analogs in Delaware, while others are arguably more protective of directors than Delaware. Texas is highly focused on its development as a corporate law jurisdiction, a deep corporate bar and has a large number of public companies headquartered in the state that could be candidates for re-domiciling. Corporate managers may want to seriously consider Texas as a choice for incorporation or re-domiciling of both public and private companies.<sup>126</sup> ■

119 TGC § 25A.004.

120 *Id.* § 25A.008.

121 *Id.* § 25A.009.

122 Goodwin, *supra* note 118.

123 Delaware provides for equitable tolling. See *IAC/InterActiveCorp v. O'Brien*, 26 A.3d 174, 177-78 (Del. 2011).

124 TGC § 25A.007.

125 Goodwin, *supra* note 118.

126 It is worth noting that, on 17 February 2025, as this article was being completed, legislation to amend the DGCL was introduced to the Delaware General Assembly intended to address criticism with respect to Delaware case law developments regarding the liability of corporate controllers, in particular, among other related matters addressed in this article.