The Relevance of Commercial Reality in Interpreting Charters and Bylaws

By Robert B. Greco and Brian T.M. Mammarella

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Recognizing that corporate charters and bylaws reflect a contract between the corporation and its stockholders, directors, and officers, Delaware courts interpret these governing documents using general principles of contract interpretation, one of which directs the court to read the instrument as a whole. Relatedly, under Delaware's objective theory of contracts, the goal of contract construction is to discern the parties' intent from the perspective of an objective, reasonable third party. Thus, where a literal reading yields a result at odds with what the drafters would have reasonably intended (which itself derives from the commercial context evidenced in plain terms throughout the instrument), literal meaning gives way to a more nuanced "objective" meaning. This article explores the application of this key precept in the interpretation of charters and bylaws.

Chicago Bridge & Iron v. Westinghouse Electric, 166 A.3d 912 (Del. 2017), exemplifies this approach. There, the Delaware Supreme Court interpreted an agreement to sell a subsidiary formed to build nuclear power plants. The initial purchase price was $0, subject to a post-closing adjustment obligating buyer to make a post-closing payment if the subsidiary's net working capital exceeded a target and seller to make a payment in the event of a shortfall. In exchange, buyer's sole remedy for seller's breach of its representations was to refuse to close and buyer agreed to indemnify seller for the subsidiary's historical liabilities. After closing, buyer claimed that it was owed nearly $2 billion from seller under the post-closing adjustment, which amounted to the difference between seller's working capital estimates (which were allegedly not GAAP compliant) and buyer's calculation (which was allegedly GAAP compliant). In rejecting buyer's claim, the court explained that contracts must be construed in a manner that honors the parties' "basic business relationship" and gives "sensible life to a real-world contract." Id. at 913–14, 927. Reading the agreement's provisions in concert, the court concluded that the deal's thesis was to allow seller to rid itself of a risky and expensive venture in exchange for (potentially) $0, a chance for upside, and a guarantee of minimal liabilities. Accordingly, the court concluded that the agreement unambiguously forbade using the post-closing adjustment to effectively sue for breach of a representation and rejected the counter-intuitive result of entitling the buyer to seek a $2 billion "purchase price."

Rather than departing from the parol evidence rule, the court did not rely on extrinsic evidence and discerned the contract's objective meaning by reading it as a whole. Chicago Bridge thereby illustrates the importance and doctrinal means of conducting a "smell test" on whether a proffered construction could reasonably reflect the drafters' intent, in which an assessment of the interpretation's commercial sensibility is subsumed. As this approach recognizes, context may inform the meaning of terms with established dictionary definitions, as Delaware law champions the meaning the parties intended above the meanings terms may have in other contexts.

But as two recent cases interpreting charter and bylaw provisions illustrate, the literal meaning of the terms used by the parties is often highly probative of their intent. In *Brown v. Matterport*, 2022 WL 89568 (Del. Ch. Jan. 10, 2022), aff'd, — A.3d —, 2022 WL 2960331 (Del. July 27, 2022) (TABLE), the Delaware Court of Chancery interpreted a 180-day lock-up imposed by a SPAC's bylaws in connection with the SPAC's initial business combination. In finding the lock-up's transfer restrictions inapplicable to shares issued in the business combination to the target's former CEO, the court explained that, under the bylaw's literal terms, the restrictions only applied to shares held "immediately following” the transaction. The court reasoned that because the former CEO did not return documentation necessary to receive his shares for over three months after closing, he did not hold shares “immediately following” the transaction and allowed him to avoid the lock-up as a result of his own tardiness. While the court explained that its interpretation of the bylaw was reasonable because the lock-up still applied to target stockholders who received shares within several days of closing, its opinion did not expressly examine the commercial sensibility of this distinction—which only subjected diligent stockholders to the lock-up and allowed others to unilaterally avoid it by belatedly returning their documentation—or whether the lock-up’s drafters could have reasonably intended to draw such a distinction.

In *Stream TV Networks v. SeeCubic*, — A.3d —, 2022 WL 2149437 (Del. June 15, 2022), the Delaware Supreme Court held that a consent right in a corporate charter applied to the negotiated transfer of all of the corporation’s assets to satisfy secured creditors in a “private foreclosure.” Although the consent right was not necessarily invoked by the pledge of the same assets to the same creditors to secure the same debts, the Supreme Court explained that the consent right expressly extended to asset “sales, leases or other dispositions” and “plainly encompassed” the private foreclosure given the breadth of the phrase “other disposition.” In focusing on “disposition,” the court’s decision did not expressly address whether the consent right’s inclusion of “other dispositions,” alongside other terms that extended the consent right to transfers of “intellectual property” and grants of “exclusive licenses,” may have been intended to clarify its application to intellectual property transactions that could fall outside of the comparatively narrow “sale, lease or exchange” language used in Section 271 of the DGCL. Arguably, these deviations from Section 271, considered alongside the commercial context, could reasonably be read to serve this purpose rather than applying to an unlikely transfer of pledged assets in a private foreclosure.

The adoption of relatively literal interpretations in *Matterport* and *Stream TV Networks*, contrasted against the *Chicago Bridge* analysis, serves as a reminder that, in many cases, terms’ traditional meanings serve as more compelling indicia of intent than context and commercial reality that may (or may not) be apparent on the instrument’s face. *Matterport* and *Stream TV Networks* do not, however, undermine applying the principles applied in *Chicago Bridge* to the interpretation of charter and bylaw provisions. Despite these principles’ limited application in *Matterport* and *Stream TV Networks*, the unique contractual terms in each case may not have revealed the drafters’ objective intent as readily as the agreement in *Chicago Bridge*, which the Supreme Court found could not support a $2 billion payment to a buyer who acquired nuclear power plants for $0 at closing. Moreover, *Matterport* and *Stream TV Networks* respectively involved the interpretation of transfer restrictions and enhanced voting requirements, both of which are more strictly construed under Delaware law. Accordingly, considerations of commercial sensibility could carry less weight in interpreting these types of provisions, but feature more prominently in construing other charter and bylaw provisions. While charter and bylaw provisions are not always the result of the same degree of bilateral negotiation as other commercial contracts, particularly for public corporations, an approach that favors the drafters’ intent and commercial reality offers real-life benefits by, among other things, preserving parties’ expectations and mitigating, at least in part, the need to draft governing documents with increasing verbosity to specifically address myriad potential issues. And streamlining charter and bylaw provisions provides practical benefits to corporations by reducing legal costs and assisting investors and courts in interpreting comparatively cleaner language. Accordingly, while drafters may wish to err on the side of caution, the consideration of commercial reality endorsed in Chicago Bridge should continue to have a role in the interpretation of charter and bylaw provisions.

Robert B. Greco *(greco@rlf.com) and* ***Brian T.M. Mammarella*** *(mammarella@rlf.com) are associates of Richards, Layton & Finger. Their practice focuses on transactional matters involving Delaware corporations, including mergers*

and acquisitions, corporate governance, and corporate finance. The views expressed in this article are those of the authors and not necessarily those of Richards, Layton & Finger or its clients.