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Shawe v. Elting: The Imperfect Sale of TransPerfect Global, Inc.

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Note

SHAWE v. ELTING: THE IMPERFECT SALE OF TRANSPERFECT GLOBAL, INC.

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INTRODUCTION

In *Shawe v. Elting*,[1] the Delaware Supreme Court held that the Court of Chancery properly exercised its equitable powers under Delaware's custodian statute when, upon finding the presence of shareholder and director deadlock, it appointed a custodian to sell a massively profitable corporation to a third party.[2] Phillip Shawe and Elizabeth Elting were the co-founders, co-CEOs, and the only two directors of TransPerfect Global, Inc.[3] The closely held corporation was structured such that Shawe and Elting behaved as fifty-fifty owners of the company.[4] In the absence of a written agreement governing the rights of stockholders,[5] the personal and business relationships between Shawe and Elting devolved into irresolvable dysfunction, and the parties were left with no intra-corporate recourse.[6] In the litigation that ensued, the Court of Chancery found that the deadlock between Shawe and Elting satisfied the threshold requirements of Section 226 of the Dela-

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1. 157 A.3d 152 (Del. 2017).

2. *Id.* at 160.

3. *In re* Shawe & Elting LLC, No. 9661-CB, No. 9686-CB, No. 9700-CB, No. 10449-CB, 2015 Del. Ch. LEXIS 211, at *4 (Del. Ch. Aug. 13, 2015), *aff'd sub nom.* Shawe v. Elting, 157 A.3d 152 (Del. 2017).

4. *Id.* at *6.

5. *Id.* at *9.

6. *See* discussion *infra* Part I.B.

ware General Corporation Law ("DGCL")[7] and appointed a custodian to force a sale of the multi-million dollar corporation to a third party, despite Shawe's objections.[8] The Delaware Supreme Court affirmed the decision, holding that the custodian statute's grant of power was broad enough to authorize the Court of Chancery to issue such a remedy.[9]

The Delaware Supreme Court erred in two respects. First, the court affirmed the Court of Chancery's expansive reasoning with respect to the "irreparable harm" requirement of Section 226(a)(2).[10] In doing so, it ignored longstanding jurisprudence requiring a demonstration of imminent insolvency or loss of revenue to the corporation in question, and instead accepted the Court of Chancery's proposition that irreparable harm may encompass things like severely diminished employee morale, client skepticism, and failure to benefit from proposed acquisitions.[11] The court focused on this erroneous interpretation of irreparable harm expansively, despite the fact that custodianship was warranted regardless under Section 226(a)(1).[12] This Note argues that this nonessential dictum seems to have been used to illustrate some degree of proportionality between the alleged harm to the corporation and the extremity of the remedy ordered.[13]

Second, the court improperly affirmed the Court of Chancery's grant of expansive custodial authority.[14] Section 226 jurisprudence indicates the reluctance with which Delaware courts have ordered the intrusive custodianship remedy, and emphasizes the principle that a custodian's authority should be as narrowly tailored as possible.[15] The court accepted a custodial sale as the only means of appropriate relief without first implementing viable alternative remedies.[16] Further, in holding as it did, the court failed to recognize that the language and prior application of Section 226 does not provide stockholders with notice that a remedy as drastic as a forced sale of their company might occur, absent their consent.[17]

7. *See* DEL. CODE ANN. tit. 8, § 226(a) (1953).
8. *In re Shawe & Elting LLC*, 2015 Del. Ch. LEXIS 211, at *106.
9. Shawe v. Elting, 157 A.3d 152, 160 (Del. 2017).
10. *See* discussion *infra* Part IV.A.
11. *See* discussion *infra* Part IV.A.
12. *See* discussion *infra* Part IV.A.
13. *See* discussion *infra* Part IV.A.
14. *See* discussion *infra* Part IV.B.
15. *See* discussion *infra* Part IV.B.
16. *See* discussion *infra* Part IV.B.
17. *See* discussion *infra* Part IV.B.

I. THE CASE

A. The Company and the Parties

In re Shawe & Elting LLC[18] concerned TransPerfect Global, Inc. ("TransPerfect" or "the Company"), a Delaware corporation specializing in translation services, website localization, and litigation support.[19] The Company's breadth is global, spanning ninety-two offices in eighty-six cities worldwide and employing more than 3,500 full-time employees.[20] In 2014, after a period of steadily profitable growth, the Company's revenue exceeded an all-time high of $470 million, and its net income totaled $79.8 million.[21]

Elizabeth Elting and Philip Shawe—formerly engaged to be married—founded the Company and served as its co-CEOs.[22] They also served as the only two members of the board of directors.[23] Of the Company's 100 shares of common stock, Elting owned fifty, Shawe owned forty-nine, and Shawe's mother, Shirley Shawe ("Ms. Shawe") owned the remaining share.[24] Shawe treated his mother's share as his own,[25] and the court found that Shawe and Elting "behaved functionally at all times relevant to this case as if they were 50-50 owners of [the Company]."[26] Shawe and Elting "never entered into any written agreements governing the operations of the Company or their relationship as stockholders, such as a buy/sell agreement."[27] Shawe and Elting led separate service divisions, and their respective divisions accounted for roughly equal percentages of the company's revenue in 2013 and 2014.[28]

18. No. 9661-CB, No. 9686-CB, No. 9700-CB, No. 10449-CB, 2015 Del. Ch. LEXIS 211 (Del. Ch. Aug. 13, 2015).

19. *Id.* at *4.

20. *Id.* TransPerfect also maintains a network of more than 10,000 translators, editors, and proofreaders working in approximately 170 different languages. *Id.*

21. *Id.* at *10.

22. *Id.* at *4.

23. *Id.*

24. *Id.* at *4–5.

25. *Id.* at *5. The court observed that, in 2014, "[Shawe] held a proxy giving him the 'full and complete power to exercise at any time . . . any and all rights to and/or arising from or connected with' [his mother's] share of [the Company]." *Id.*

26. *Id.* at *6.

27. *Id.* at *9.

28. *Id.*

B. A Timeline of Events: Tensions, Disagreements, and "Mutual Hostaging"

Tensions between Shawe and Elting began as early as their broken engagement in 1997, five years after they founded the Company in their college dormitory room.[29] When Elting ended her relationship with Shawe, Shawe began acting bizarrely—his behavior included crawling under Elting's bed and staying there for a period of time, showing up unannounced at Elting's hotel room in Argentina, and inviting himself to Elting's wedding in Jamaica.[30] Personal differences bled into Shawe and Elting's professional relationship, and early disagreements began over things such as the way company assets were spent[31] and the proposed opening of global satellite offices.[32] By late 2012, the disagreements between Shawe and Elting escalated into what Shawe described as "mutual hostaging," a process by which "Elting would hold things up that Shawe wanted unless she got certain things that she wanted, and vice versa."[33] In November of 2012, for example, Elting rejected the proposed acquisition of a company called Rixon—despite its value to TransPerfect[34]—when Shawe declined to approve a $10 million non-tax distribution requested by Elting.[35] Further, though "board-level decisions" historically required the approval of both CEOs, the relationship between the two deteriorated such that Elting "insisted that routine decisions must receive their 'dual approval.'"[36]

The pattern of "mutual hostaging" between the two CEOs continued into 2013, at which point there still existed no buy/sell agreement.[37] In ear-

29. *Id.* at *7.

30. *Id.* at *7–8 n.12.

31. *Id.* at *10–11. Disagreement of this nature occurred in 2011 when Elting learned that Shawe spent some of the Company's American Express membership points on an expensive plane ticket for his fiancée without her approval. *Id.* Elting also "became upset when she learned that Shawe had submitted raises for certain employees without her approval." *Id.* at *12.

32. *Id.* at *13–14. One particularly heated exchange occurred in 2012, when Elting rejected Shawe's proposal to open an office in France because of the area's employment laws. *Id.* In response, Shawe threatened to freeze the Company's accounts and shut down the Company. *See id.* at *14 (quoting heated emails from Shawe to Elting). Ultimately, Elting relented to Shawe's request. *Id.*

33. *Id.* at *15.

34. The Company's head of sales referred to the acquisition as "fantastic" and implored Elting to "please . . . not derail that one." *Id.* at *16.

35. *Id.* at *15.

36. *Id.* at *17–18. The dual approval requirement resulted in cross-division meddling. *Id.* at *18. In other words, Shawe would meddle with the demands that Elting had for her respective division (such as raises for certain employees within her umbrella of leadership), and vice versa. *Id.*

37. *Id.* at *22. A buy/sell agreement governs shareholder exits in a closely held business by "provid[ing] a firm method of liquidating a shareholder's interest upon appropriate events." Kerry M. Lavelle, *Drafting Shareholder Agreements for the Closely-Held Business*, 4 DEPAUL BUS. L.J. 109, 111 (1991).

ly October of 2013, Shawe threatened to terminate Gale Boodram, the Company's payroll manager,[38] if she executed a wire transfer to make a distribution to the Company's stockholders without his consent—an act endorsed by Elting.[39] Elting retaliated by terminating the Company's Chief Operating Officer, who she claimed had interfered with the wire transfer.[40] Subsequently, Elting retained a corporate lawyer to help her communicate with Shawe and suggested that Shawe do the same.[41] Shawe belittled Elting's proposal as "her latest tantrum" and an idea that was "batsh*t crazy."[42] Shawe then terminated the "Company's real estate broker [of] twenty years"—an "obvious retaliation," since Elting's husband was in the broker's employ.[43] Countless feuds and another failed compromise later, Shawe began to surreptitiously monitor Elting's private emails.[44] Shawe repeatedly and secretly entered Elting's locked office in her absence to dismantle her computer, remove and copy its hard drive, and then reinstall it.[45] He further "arranged to access the hard drive on her office computer remotely."[46]

Shawe and Elting's corporate in-fighting persisted, resulting in deadlock over expenses not approved by both parties,[47] personal legal representation,[48] and employee hiring and compensation processes.[49] One of the consequences of such deadlock was the double payment of Elting's taxes by the Company,[50] apparently attributable to the fact that "Shawe and Elting

38. Shawe repeatedly accused Boodram of showing favoritism to Elting and viewed her as "Elting's 'puppet.'" *In re Shawe & Elting LLC*, 2015 Del. Ch. LEXIS 211, at *24, *29.

39. *Id.* at *30.

40. *Id.*

41. *Id.* at *31.

42. *Id.*

43. *Id.*

44. *Id.* at *40.

45. *Id.* at *40–41.

46. *Id.* at *41. Through Shawe's "stealthy actions," he accessed approximately 19,000 of Elting's emails, including approximately 12,000 privileged communications with her personal counsel in this litigation. *Id.* at *42.

47. *See id.* at *44–45 (explaining that Shawe refused to participate in the Company's "true-up process," a process by which (1) all unagreed-upon expenses incurred by both CEOs were tallied and (2) proportional distributions in the form of additional compensation were made to each party).

48. *See id.* at *47–48 (explaining that Shawe retained the Company's outside counsel "to represent him personally in his dispute with Elting" while "incredibly claim[ing] not to see any conflict").

49. *See id.* at *51–53 (explaining that Shawe (1) unilaterally hired a senior executive into one of Elting's divisions despite Elting's objections and (2) authorized a finance manager to provide certain employee raises without obtaining Elting's approval).

50. TransPerfect was reorganized in 2007 as a Subchapter S corporation. *Id.* at *8. Instead of paying federal income taxes, Subchapter S corporations' income or losses "are divided among and passed through to its stockholders in proportion to their holdings." *Id.* Stockholders must

were incapable of behaving rationally."[51] Another consequence was the termination of the Company's relationship with its public relations firm—a replacement for which Shawe and Elting were subsequently unable to agree upon.[52] Finally, in May of 2014, the Shawe-Elting feud culminated in four separate lawsuits which they filed against each other.[53]

C. Brief Procedural History

On May 23, 2014, Elting petitioned the Delaware Court of Chancery to (1) appoint a custodian to sell the Company under Section 226(a)(2) of the DGCL[54] or (2) equitably dissolve the Company.[55] Several months later, pursuant to Section 211 of the DGCL,[56] Elting filed an action to compel the Company to hold an annual stockholder's meeting ("the Section 211 Action").[57] To resolve the Section 211 Action, the parties[58] "stipulated that they were deadlocked on electing directors."[59] Subsequently, Elting filed another action under Section 226(a)(1) of the Delaware Code,[60] seeking "the appointment of a custodian or receiver to act in the best interests of [the Company] given the stipulated deadlock among the Company's stockholders over the election of directors."[61] After a six-day trial in February of 2015, the Court of Chancery appointed a corporate attorney as a mediator to negotiate a resolution between the two parties.[62] Shawe and Elting were

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then report the income or loss on their personal income tax returns and are compensated by the corporation with pro rata tax distributions. *Id.*

51. *Id.* at *55.

52. *Id.* at *56.

53. *Id.* at *56–57.

54. *See* DEL. CODE ANN. tit. 8, § 226(a)(2) (1953) ("The Court of Chancery, upon application of any stockholder, may appoint 1 or more persons to be custodians . . . of and for any corporation when . . . [t]he business of the corporation is suffering or is threatened with irreparable injury because the directors are so divided respecting the management of the affairs of the corporation that the required vote for action by the board of directors cannot be obtained and the stockholders are unable to terminate this division . . . ."); *see also* discussion *infra* Part III.A.2.

55. *In re Shawe & Elting LLC*, 2015 Del. Ch. LEXIS 211, at *57.

56. *See* DEL. CODE ANN. tit. 8, § 211(c) (1953) ("If there be a failure to hold the annual meeting [of stockholders] . . . the Court of Chancery may summarily order a meeting to be held upon the application of any stockholder or director.").

57. *In re Shawe & Elting LLC*, 2015 Del. Ch. LEXIS 211, at *73.

58. The parties are defined as Elting, Shawe, and Ms. Shawe, who was firmly aligned with her son. *Id.* at *2, *73–74.

59. *Id.* at *73.

60. *See* DEL. CODE ANN. tit. 8, § 226(a)(1) (1953) ("The Court of Chancery, upon application of any stockholder, may appoint 1 or more persons to be custodians . . . of and for any corporation when[, a]t any meeting held for the election of directors the stockholders are so divided that they have failed to elect successors to directors whose terms have expired or would have expired upon qualification of their successors . . . ."); *see also* discussion *infra* Part III.A.1.

61. *In re Shawe & Elting LLC*, 2015 Del. Ch. LEXIS 211, at *74–75.

62. *Id.* at *79.

given until June 30, 2015 to resolve their differences under the mediator's supervision,[63] but were unable to reach an agreement by that date.[64]

D. The Court of Chancery's Reasoning and Holding

The Court of Chancery ultimately held that the appointment of a custodian to oversee a judicially ordered sale of the Company was warranted both under Sections 226(a)(1) and 226(a)(2).[65]

The Court of Chancery observed that the requirements of 226(a)(1)—a provision which does not require a showing of irreparable injury—were plainly met.[66] The court reasoned that, since the stockholders of TransPerfect expressly stipulated to deadlock and an inability to elect successor directors,[67] the 226(a)(1) mandate was satisfied.[68] Though the fulfillment of the 226(a)(1) mandate is enough to authorize the court to exercise its discretion and appoint a custodian, Chancellor Bouchard continued his inquiry under 226(a)(2).[69] He observed that Section 226(a)(2) carries three conditions that must be satisfied before the Court of Chancery may exercise its authority under the statute.[70] First, the directors must be deadlocked.[71] Second, the corporation's business must either be suffering or be threatened with irreparable injury because of the deadlock.[72] Third, the "circumstances must be such that the shareholders are unable by shareholder vote to terminate the division between the directors."[73] The Court of Chancery ultimately held (1) that Shawe and Elting were "deadlocked on several matters of critical importance to the Company" including tax and non-tax distributions and the hiring and retention of various employees;[74] (2) that irreparable in-

63. *Id.* at *79–80.

64. *Id.* at *80.

65. *Id.* at *105. The Court of Chancery also held (1) the equitable dissolution of the Company was inappropriate in the circumstances before the court, (2) that Elting was entitled to favorable judgment with respect to each of the claims Shawe asserted against her, and (3) that the LLC founded by Shawe and Elting should be dissolved. *Id.* at *114–15, *126, *133. Considering the issues on appeal, this Note will not address these holdings.

66. *Id.* at *82.

67. *See supra* note 59 and accompanying text.

68. *In re Shawe & Elting LLC*, 2015 Del. Ch. LEXIS 211, at *82–83.

69. *Id.* at *83.

70. *Id.* at *83–84 (citing Hoban v. Dardanella Elec. Corp., No. 7615, 1984 Del. Ch. LEXIS 599, at *2–3 (Del. Ch. June 12, 1984)).

71. *Id.* The board of directors must be "so divided respecting the management of the affairs of the corporation that the vote required for curative action by the board as a governing body cannot be obtained." *Id.* at *83–84 (quoting *Hoban*, 1984 Del. Ch. LEXIS 599, at *2).

72. *Id.* at *84 (quoting *Hoban*, 1984 Del. Ch. LEXIS 599, at *2–3).

73. *Id.* (quoting *Hoban*, 1984 Del. Ch. LEXIS 599, at *2).

74. *Id.* at *84, *89, *89 n.285.

jury[75] to a corporation has been found to include "harm to a corporation's reputation, goodwill, customer relationships, and employee morale"[76] and that it had occurred to the Company in the form of severely diminished employee morale, client skepticism, and failure to potentially benefit from proposed acquisitions;[77] and (3) that the stipulation entered into by the stockholders "plainly" demonstrated that they were unable to overcome director deadlock.[78] Thus, all three requirements of 226(a)(2) were met.

As the court observed, "Even when the requirements of Sections 226(a)(1) or 226(a)(2) have been satisfied, the appointment of a custodian is not mandatory, but is committed to the Court's discretion."[79] Thus, the court was faced with the question of whether the circumstances before it truly warranted an exercise of its authority under Section 226(a).[80] In answering this question, the court weighed three options.[81] The court first rejected the option to "decline to appoint a custodian and leave the parties to their own devices," since (1) dysfunctional management was causing the Company to suffer and threatened it with irreparable harm, and (2) "to leave Elting with no recourse except to sell her 50% interest in the Company" would not enable her to sell her stake at a fair price, since no "rational person would want to step into Elting's shoes to partner with someone willing to 'cause constant pain' and 'go the distance' to get his way."[82] The court then rejected the option to appoint a custodian as a third director in a tie-breaking role, observing that the court would be "enmesh[ed] . . . into matters of internal corporate governance for an extensive period of time."[83] The final option, which the court ultimately adopted, was to appoint a custodian to sell the company to a third party.[84] The court cited two prior instances when the Court of Chancery "appointed custodians to resolve deadlocks involving profitable corporations and authorized them to conduct a

75. *See id.* at *92–93 ("Irreparable injury exists 'when a later money damage award would involve speculation' . . . ." (quoting Hollinger Int'l, Inc. v. Black, 844 A.2d 1022, 1090 (Del. Ch. 2004), *aff'd*, 872 A.2d 559 (Del. 2005))).

76. *Id.* at *93 (citing Kirpat, Inc. v. Del. Alcoholic Beverage Comm'n, 741 A.2d 356, 358 (Del. 1998); Arkema Inc. v. Dow Chem. Co., No. 5479-VCP, 2010 Del. Ch. LEXIS 120, at *4 (Del. Ch. May 25, 2010); Penn Mart Supermarkets, Inc. v. New Castle Shopping LLC, No. 20405-NC, 2005 Del. Ch. LEXIS 199, at *15 (Del. Ch. Dec. 15, 2005); Shah v. Shah, No. 904(k), 1986 Del. Ch. LEXIS 467, at *2 (Del. Ch. Sept. 25, 1986)).

77. *Id.* at *96–98.

78. *Id.* at *98.

79. *Id.* at *99.

80. *Id.*

81. *See infra* notes 82–87 and accompanying text.

82. *In re Shawe & Elting LLC*, 2015 Del. Ch. LEXIS 211, at *101–02.

83. *Id.* at *102.

84. *Id.* at *102–03.

sale of the corporation."[85] The court reasoned that, though the remedy was "unusual" and "should be implemented only as a last resort and with extreme caution," it was appropriate to opt for a custodial sale in this circumstance, since "[Shawe and Elting's] dysfunction must be excised to safeguard the Company."[86] Shawe and his mother filed an interlocutory appeal, asking the Delaware Supreme Court to reverse and to consider "less drastic measures."[87]

II. LEGAL BACKGROUND

As a general matter, Section 226(a) of the DGCL allows the Court of Chancery to appoint a custodian in any one of three scenarios: stockholder deadlock,[88] director deadlock,[89] or the abandonment of corporate business.[90] This Part will first lay out the threshold requirements of Sections 226(a)(1) and 226(a)(2), both of which Elting used as grounds for relief.[91] It will then explain the discretionary nature of a custodial appointment under Section 226(b), and will demonstrate the level of authority the Court of Chancery has previously vested in Section 226 custodians.[92]

A. The Threshold Requirements of Sections 226(a)(1) and 226(a)(2)

1. Section 226(a)(1): The Stockholder Deadlock Scenario

Section 226(a)(1) provides that the Court of Chancery may appoint a custodian when, "[a]t any meeting held for the election of directors[,] the stockholders are so divided that they have failed to elect successors to directors whose terms have expired or would have expired upon qualification of their successors."[93] Unlike Section 226(a)(2), Section 226(a)(1) does *not* require a showing of actual or threatened irreparable corporate harm.[94] Sec-

85. *Id.* at *102 (citing Bentas v. Haseotes, 769 A.2d 70, 73 n.3 (Del. Ch. 2000); Fulk v. Wash. Serv. Assocs., No. 17747-NC, 2002 Del. Ch. LEXIS 78, at *2 (Del. Ch. June 21, 2002)).

86. *Id.* at *102–103.

87. Shawe v. Elting, 157 A.3d 152, 154–55 (Del. 2017).

88. *See* discussion *infra* Part II.A.1.

89. *See* discussion *infra* Part II.A.2.

90. *See* DEL. CODE ANN. tit. 8, § 226(a)(3) (1953) (providing that the Court of Chancery may appoint a custodian when "[t]he corporation has abandoned its business and has failed within a reasonable time to take steps to dissolve, liquidate, or distribute its assets"). For purposes of this Note, the requirements and applications of Section 226(a)(3) will not be addressed, since the petitioner in *Shawe v. Elting* made no claim for relief thereunder.

91. *See* discussion *infra* Part II.A.

92. *See* discussion *infra* Part II.B.

93. DEL. CODE ANN. tit. 8, § 226(a)(1) (1953).

94. *See* Giuricich v. Emtrol Corp., 449 A.2d 232, 238 (Del. 1982) ("Specifically, § 226(a)(1) requires no additional showing such as irreparable harm to the stockholder or the corporation.").

tion 226(a)(1) requires only a demonstration of a stockholder division resulting in failure to elect successor directors—it contains "no other condition or exception, expressed or implied."[95] Thus, a Section 226 custodial appointment is more easily pursued under 226(a)(1), since a claim thereunder is subject to fewer statutory prerequisites.[96]

2. Section 226(a)(2): The Director Deadlock Scenario

Section 226(a)(2) provides that the Court of Chancery may appoint a custodian when directors have reached a decision-making impasse that threatens the business of the corporation with irreparable injury and when such an impasse is incurable by way of shareholder vote.[97] This subsection has three distinct requirements: (1) "the business of the corporation must either be suffering or be threatened with irreparable injury," (2) "the cause of the business malady must stem directly from the fact that the directors are so divided respecting the management of the corporation's affairs that the vote required for curative action by the board as a governing body cannot be obtained," and (3) "circumstances must be such that the shareholders are unable by shareholder vote to terminate the division between the directors."[98]

Delaware's Section 226 jurisprudence indicates that irreparable harm exists where the corporation in question is threatened with insolvency or loss of revenue.[99] In *Hoban v. Dardanella Electric Corp.*,[100] the Court of Chancery found that irreparable harm existed where director deadlock was such that it prevented a change in the corporation's bank which would: (1) extend the company's line of credit by $1.1 million, (2) reduce its interest expense by $100,000, and (3) prevent the company from "go[ing] under."[101] Similarly, in *Kleinberg v. Aharon*,[102] the Court of Chancery found that a corporation suffered irreparable harm where its directors' deadlock de-

95. *Id.*

96. *See, e.g.*, Miller v. Miller, No. 2140-VCN, 2009 Del. Ch. LEXIS 16, at *10–12 (Del. Ch. Feb. 10, 2009) (finding that the claimant was unable to offer proof sufficient to support a finding of threatened or present irreparable harm under 226(a)(2) but was able to "clearly demonstrate[] that the limited statutory prerequisite" of 226(a)(1) had been satisfied); *see also* Bentas v. Haseotes, 769 A.2d 70, 73 n.3 (Del. Ch. 2000) (granting custodial relief under 226(a)(1) but noting that the stockholder division before the court had not affected the economic well-being of the still solvent and profitable company).

97. DEL. CODE ANN. tit. 8, § 226(a)(2) (1953).

98. Hoban v. Dardanella Elec. Corp., No. 7615, 1984 Del. Ch. LEXIS 599, at *2–3 (Del. Ch. June 12, 1984); *see also* Kleinberg v. Aharon, No. 12719-VCL, 2017 Del. Ch. LEXIS 24, at *32–33 (Del. Ch. Feb. 13, 2017) (listing Section 226(a)(2)'s requirements as laid out in *Hoban*).

99. *See infra* notes 100–109 and accompanying text.

100. No. 7615, 1984 Del. Ch. LEXIS 599 (Del. Ch. June 12, 1984).

101. *Id.* at *4–7.

102. No. 12719-VCL, 2017 Del. Ch. LEXIS 24 (Del. Ch. Feb. 13, 2017).

prived it of the opportunity to benefit from a business venture with another company that credibly seemed to be its "only hope" and caused its only remaining commercial relationship to disintegrate.[103] The court noted that, unless the deadlock came to an end, "the [c]ompany ha[d] no chance of pursuing a new business plan and w[ould] become irretrievably insolvent."[104]

Conversely, mere inconvenience to the company and its affairs is insufficient to establish irreparable harm.[105] In *Miller v. Miller*,[106] the Court of Chancery found that the purported deadlock between the sibling-owners of two separate youth camps operating as one company amounted to nothing but an inconvenience, because the business was still profitable and still operated "reasonably well."[107] The separate camps served as separate profit centers for each of the brothers allowing for a reasonable division of income between them, and camp managers were able to navigate logistical problems such that the daily and efficient operation of the camps remained unaffected.[108] In emphasizing the profitability of the camps, the court held that no irreparable harm existed.[109]

The second and third elements of 226(a)(2)—"that the directors must be, in fact, deadlocked"[110] and that the shareholders "must be 'unable to vote to terminate'" such deadlock by way of shareholder vote'"[111]—usually go hand-in-hand and are present most commonly in the context of closely held private corporations.[112] For example, the dispute in *Hoban* involved a company with two equally situated shareholders, Hoban and Rensberger, who doubled as the company's only two directors.[113] When Hoban proposed a purportedly essential bank transition,[114] Rensberger refused to give his approval unless Hoban, *inter alia*, resigned as CEO, thus creating an impasse.[115] Because of the dual nature of their roles, the director deadlock

103. *Id.* at *17–18, *24–26, *35, *37.

104. *Id.* at *39.

105. *See infra* notes 106–109 and accompanying text.

106. No. 2140-VCN, 2009 Del. Ch. LEXIS 16 (Del. Ch. Feb. 10, 2009).

107. *Id.* at *9.

108. *Id.*

109. *Id.* at *9–10.

110. Kleinberg v. Aharon, No. 12719-VCL, 2017 Del. Ch. LEXIS 24, at *32 (Del. Ch. Feb. 13, 2017) (citing *In re* Shawe & Elting LLC, No. 9661-CB, No. 9686-CB, No. 9700-CB, No. 10449-CB, 2015 Del. Ch. LEXIS 211, at *26 (Del. Ch. Aug. 13, 2015), *aff'd sub nom.* Shawe v. Elting, 157 A.3d 152 (Del. 2017)).

111. *Id.* at *32–33 (quoting Hoban v. Dardanella Elec. Corp., No. 7615, 1984 Del. Ch. LEXIS 599, at *1 (Del. Ch. June 12, 1984)).

112. *See infra* notes 113–121 and accompanying text.

113. Hoban v. Dardanella Elec. Corp., No. 7615, 1984 Del. Ch. LEXIS 599, at *3 (Del. Ch. June 12, 1984).

114. *See supra* note 101 and accompanying text.

115. *Hoban*, 1984 Del. Ch. LEXIS 599, at *5–6.

was incurable by way of a shareholder vote,[116] and—having found a threat of irreparable harm to be present[117]—the court appointed a custodian under 226(a)(2).[118] Similarly, the company involved in *Miller* was owned and managed by two brothers, each holding fifty percent of its stock.[119] Due to mounting tensions and a failure to elect directors for more than five years, the two siblings were held over as the company's only two directors, "thereby preserving an even split . . . consistent with the equal ownership interests."[120] The deadlock in *Miller*, therefore, could not have been cured by shareholder vote.[121]

Importantly, Section 226(a) provides that the Court of Chancery "*may* appoint" a custodian where its statutory prerequisites are met.[122] This language has been interpreted as conferring broad judicial discretion—thus, even where 226(a) has been satisfied, the court is not compelled to provide the custodianship remedy.[123] Delaware courts have traditionally demonstrated reluctance in ordering the "intrusive" custodianship remedy,[124] since "such relief constitutes a radical step that ought not to be granted unless the plaintiff has rather plainly shown his entitlement to it."[125]

116. *See id.* at *7 ("Since the two directors are each a 50 per cent shareholder of the corporation, it follows that the division of the board which threatens irreparable injury to [the company] cannot be cured by action of the shareholders.").

117. *See supra* note 101 and accompanying text.

118. *Hoban*, 1984 Del. Ch. LEXIS 599, at *7.

119. Miller v. Miller, No. 2140-VCN, 2009 Del. Ch. LEXIS 16, at *3 (Del. Ch. Feb. 10, 2009).

120. *Id.* at *7.

121. *Id.* Despite the presence of director deadlock, the court in *Miller* observed that the corporation was not threatened with irreparable harm as required by 226(a)(2). *Id.* at *9. Thus, the court granted custodial relief under Section 226(a)(1), since there was "an undisputed showing of utter disagreement between the two 50% stockholder factions on a number of serious issues." *Id.* at *11–12.

122. *See* DEL. CODE ANN. tit. 8, § 226(a) (1953) (emphasis added).

123. *See Miller*, 2009 Del. Ch. LEXIS 16, at *13 n.15 ("Significantly, the Court 'may' appoint a custodian if the conditions of 8 Del. C. § 226 are satisfied; it is not mandatory."); *see also* Kleinberg v. Aharon, No. 12719-VCL, 2017 Del. Ch. LEXIS 24, at *33 (Del. Ch. Feb. 13, 2017) ("The decision to appoint a custodian is a matter of the court's discretion." (quoting 1 EDWARD P. WELCH ET AL., FOLK ON THE DELAWARE GENERAL CORPORATION LAW § 226.01, at 7-308 (6th ed 2015))).

124. *See* Bentas v. Haseotes, 769 A.2d 70, 77 (Del. Ch. 2000) (explaining defendants' argument that "the intrusive custodianship remedy ought not to be granted, especially for an economically successful corporation . . . , unless the record clearly shows that it is necessary and there is no better alternative").

125. Giancarlo v. OG Corp., No. 10669, 1989 Del. Ch. LEXIS 75, at *7–8 (Del. Ch. June 23, 1989); *see, e.g.*, Bentas v. Haseotes, No. 17223, 1999 Del. Ch. LEXIS 205, at *15–17 (Del. Ch. Nov. 5, 1999) (declining to appoint a custodian in the first instance and instead ordering a shareholders' meeting which, in the court's opinion, had the potential to end the shareholder deadlock in dispute).

B. A Discretionary Exercise: The Scope of Custodial Authority Previously Granted by the Court of Chancery Under Section 226(b)

Section 226(b) vests the Court of Chancery with considerable authority in fashioning the powers of an appointed custodian.[126] Still, once the custodianship remedy has been ordered, "[t]he involvement of the Court of Chancery and its custodian in the corporation's business and affairs should be kept to a minimum and should be exercised only insofar as the goals of fairness and justice . . . require."[127] As the court in *Bentas v. Haseotes*[128] opined, the risk that the custodianship remedy would be unnecessarily intrusive vis-à-vis the board's management of the corporation is mitigated by specifically defining the custodian's role and the parameters of his or her authority.[129] A custodian's authority "should be tailored as narrowly as possible because judicially-supervised interference with the ordinary operation of a corporation should be kept to a minimum."[130]

In *Giuricich v. Emtrol Corp.*,[131] when the plaintiffs' petition for the appointment of a custodian was originally denied by the Court of Chancery, the Delaware Supreme Court remanded the case with instructions to appoint a custodian vested with "sharply limited" powers.[132] The impartial[133] custodian was to be given the authority to act *only* when "the board of directors . . . failed to reach a unanimous decision on any issue properly before them."[134] The custodian's "tie-breaker" decision in these instances would be binding on the corporation and its agents.[135] It was left to the Court of Chancery to determine how long the custodian would preside, unless or until *all* of the company's shareholders unanimously requested the custodian's discharge.[136]

Further, in *Miller*, the Court of Chancery appointed a custodian for a two-year term with limited authority.[137] The custodian was vested with the power:

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126. *See* DEL. CODE ANN. tit. 8, § 226(b) (1953) (defining the scope of the appointed custodian's authority "*except when the Court shall otherwise order*" (emphasis added)).

127. Giuricich v. Emtrol Corp., 449 A.2d 232, 240 (Del. 1982).

128. 769 A.2d 70 (Del. Ch. 2000).

129. *Id.* at 78.

130. Miller v. Miller, No. 2140-VCN, 2009 Del. Ch. LEXIS 16, at *14 (Del. Ch. Feb. 10, 2009).

131. 449 A.2d 232 (Del. 1982).

132. *Id.* at 240.

133. *See id.* at 240 n.15 (stating that the custodian should not be a stockholder or creditor of the corporation or of any of its subsidiaries or affiliates).

134. *Id*. at 240.

135. *Id.*

136. *Id.*

137. Miller v. Miller, No. 2140-VCN, 2009 Del. Ch. LEXIS 16, at *18–19 (Del. Ch. Feb. 10, 2009).

> (1) to break material deadlocks between directors; (2) to resolve operational deadlocks between the two camps; (3) to participate with the power of a director in the event one of the directors is unable to serve, with such action duly to reflect the interest of the director for whom the custodian is substituting; and (4) to seek to resolve the impasse over the future of the Company.[138]

The custodian would serve a "tie-breaking" role similar to that of the custodian in *Giuricich*,[139] with additional mediation powers—however, "no authority [was] conferred upon the custodian[] to sell or divide the Company's real property."[140] Despite its holding, the Court of Chancery nonetheless invited counsel on both sides to confer and to jointly propose different scopes of custodial authority for its consideration and to suggest an individual to serve as the company's custodian.[141]

Even in *Bentas*, where the Court of Chancery vested rather broad power in the custodian to "explore any and all alternatives that might result in a mutually agreed solution to the current shareholder deadlock,"[142] it expressly declined to prescribe the method through which the custodian would seek to end the deadlock.[143] The court agreed with the plaintiffs that to do so would be "premature and could truncate the parties' ability to explore additional solutions that may lead to an agreed resolution of their differences."[144] In its reasoning, the court refused to consider the defendants' proposal that the custodian "be directed and empowered to sell the Company to a third party."[145] Additionally, while the custodian would have the authority to cast a tie-breaking vote, the custodian would *only* be able to do so "in disputes that the custodian deem[ed] to be significant to managing the corporation's business and affairs"—not on *every* issue with regard to which the board is equally divided.[146]

III. THE COURT'S REASONING

In *Shawe v. Elting*,[147] the Delaware Supreme Court affirmed the Delaware Court of Chancery's order, holding that the court's decision to appoint

138. *Id.*

139. *See supra* notes 134–135 and accompanying text.

140. *Miller*, 2009 Del. Ch. LEXIS 16, at *19 n.21.

141. *Id.* at *19. This joint proposal would be submitted by counsel as "a form of order to implement [the court's] letter opinion." *Id.*

142. Bentas v. Haseotes, 769 A.2d 70, 80 (Del. Ch. 2000).

143. *Id.*

144. *Id.*

145. *Id.* at 79.

146. *Id.*

147. 157 A.3d 152 (Del. 2017).

a custodian to sell the Company was statutorily permissible and was not an abuse of discretion, since the court reasonably concluded that other less intrusive measures to resolve director deadlock would be ineffective.[148] On appeal, Shawe made three arguments: (1) that the court exceeded its statutory authority under Section 226 when it ordered the custodian to sell a solvent company;[149] (2) that, even if the statutory authority existed to empower the custodian to sell the Company, the court should have pursued other means to address the deadlock before resorting to a sale;[150] and (3) that the United States and Delaware Constitutions do not authorize the court to order the custodian to sell the Company over stockholders' objections.[151] In a split en banc decision, the Delaware Supreme Court rejected all three of these arguments.[152] Dissenting from the majority decision of her four colleagues, Justice Valihura argued that the sale of the Company absent stockholder consent was too drastic a measure in light of applicable case law, stockholder property rights, and due process protections.[153]

On appeal, Shawe did not contest the Court of Chancery's ruling that the requirements of Section 226(a)(1) were met[154]—instead, he challenged the appointment of a custodian under Section 226(a)(2), claiming that the court incorrectly applied the standard for irreparable injury.[155] The court labeled this argument "academic," since the custodial appointment was statutorily warranted under 226(a)(1) regardless.[156] Still, the court observed that the Court of Chancery correctly applied the threatened or actual irreparable injury requirement of 226(a)(2).[157] It reasoned that, were deadlock to persist, "the Company was likely to continue on the path of plummeting employee morale, key employee departures, customer uncertainty, damage to the Company's public reputation and goodwill, and fundamental inability to grow the Company through acquisitions."[158]

148. *Id.* at 160, 166–67.

149. *Id.*

150. *Id.* at 162.

151. *Id* at 168. The court dismissed this constitutional argument and refused to consider it on the merits, since it was raised for the first time on appeal and was not "fairly presented to the trial court." *Id.* (citing DEL. SUPR. CT. R. 8). This Note will not address the constitutional argument.

152. *Id.* at 162–63, 166, 169.

153. *Id.* at 169–88 (Valihura, J., dissenting).

154. *Id.* at 161 (majority opinion); *see id.* (explaining that Shawe could not have challenged the Court of Chancery's ruling with respect to 226(a)(1), since Shawe and Elting "stipulated to the stockholder deadlock required by the statute").

155. *Id.*

156. *See id.* ("[T]he argument is academic because Shawe agreed that the Court of Chancery was authorized to appoint a custodian under § 226(a)(1).").

157. *Id.*

158. *Id.* at 162.

Shawe also argued that the Court of Chancery abused its discretion in that it did not sufficiently consider less intrusive measures before it appointed a custodian to sell the Company.[159] The Delaware Supreme Court rejected this argument based on its observation that the Court of Chancery made two attempts at developing a remedy less extreme than a company sale: (1) it appointed a custodian immediately post-trial to mediate the dispute between Shawe and Elting, which failed to resolve the deadlock,[160] and (2) it weighed the option of appointing a custodian as a third director who would serve as a "tie-breaker," and then reasonably rejected it on the grounds that the court would have to "exercise essentially perpetual oversight over the internal affairs of the Company," something it was not willing to undertake.[161] The Delaware Supreme Court ultimately observed that "[t]he Chancellor was in the best position to assess the viability of options short of sale."[162] Further, the court pointed to several cases "confirm[ing] the Court of Chancery's broad authority under the statute, which includes ordering a sale."[163]

In her dissent, Justice Valihura pointed to two main principles undermining the majority's decision.[164] First, the DGCL treats stock as personal property, which is "generally subject to traditional property law policies favoring free alienation."[165] In her analysis of the DGCL statutory scheme, Justice Valihura concluded that stockholders' personal property rights are not meant to be abridged by mere implication—rather, where the DGCL restricts the free transferability or alienability of stock, "it does so expressly."[166] Because Section 226 fails to provide express fair notice to stock-

159. *Id.* at 166.

160. *Id.* at 166–67.

161. *Id* at 167 (quoting *In re* Shawe & Elting LLC, No. 9661-CB, No. 9686-CB, No. 9700-CB, No. 10449-CB, 2015 Del. Ch. LEXIS 211, at *102 (Del. Ch. Aug. 13, 2015), *aff'd sub nom.* Shawe v. Elting, 157 A.3d 152 (Del. 2017)); *see id.* ("[T]he appointment of a custodian to act as a constant monitor and tie-breaker . . . would itself be expensive, cumbersome, and very intrusive.").

162. *Id.*

163. *Id.* at 163 & n.36 (citing Bentas v. Haseotes, 769 A.2d 70, 73 n.3 (Del. Ch. 2000); Bentas v. Haseotes, No. 17223, 2003 Del. Ch. LEXIS 24 (Del. Ch. Mar. 27, 2003); Fulk v. Wash. Serv. Assocs., No. 17747-NC, 2002 Del. Ch. LEXIS 78 (Del. Ch. June 21, 2002); *In re* Supreme Oil Co., Inc., No. 10618-VCL, 2015 Del. Ch. LEXIS 319 (Del. Ch. May 22, 2015); Brown v. Rosenberg, No. 833, 1981 Del. Ch. LEXIS 629 (Del. Ch. Dec. 17, 1981)).

164. *Id.* at 170–71 (Valihura, J., dissenting).

165. *Id.* at 170.

166. *Id.* at 173. Justice Valihura cites several examples, including Section 251 (providing notice to stockholders objecting to a merger that their shares may be subject to divestiture upon merger majority approval), Section 273 (providing notice to fifty-fifty shareholders that in the presence of threshold circumstances, their venture may be dissolved despite one shareholder's objection), and Section 303 (allowing a corporation filing for bankruptcy to, *inter alia*, "make any change in its . . . capital stock" or "be dissolved"). *Id.* at 173–75 (citing DEL. CODE ANN. tit. 8, § 251 (1953); DEL. CODE ANN. tit. 8, § 273 (1953); DEL. CODE ANN. tit. 8, § 303 (1953)).

holders that they may be subject to giving up their shares over their objection, it is unlikely that the Delaware General Assembly intended to permit the Court of Chancery to order the whole sale of a company to a third party, despite the absence of unanimous shareholder consent.[167] The second principle proffered by Justice Valihura was that "the involvement of the Court of Chancery and court-appointed custodians in a corporation's business and affairs should be kept to a minimum."[168] She explained that the Court of Chancery's past decisions illustrate the concept that the court should intrude as little as possible into the business of the corporation.[169] She further reasoned that stockholder consent to a court-issued remedy is of critical importance—it "softens the blow," so to speak, and affects the extent to which a remedy intrudes upon a corporation's affairs.[170] Absent stockholder consent, there is more intrusion.[171] Justice Valihura finally concluded that "the sale of the Company, absent stockholder consent, is too drastic a measure, and . . . the trial court should [have] consider[ed the] implementation of remedies on an incremental basis."[172]

IV. ANALYSIS

In affirming the Court of Chancery's decision, the Delaware Supreme Court erred in two ways. First, the court affirmed the Court of Chancery's incorrect reasoning with respect to the "irreparable harm" requirement of Section 226(a)(2).[173] It ignored longstanding jurisprudence requiring a demonstration of imminent insolvency or loss of revenue, and instead accepted the Court of Chancery's expansive proposition that irreparable harm may be deemed to encompass severely diminished employee morale, client skepticism, and failure to benefit from proposed acquisitions.[174] Second, the court improperly affirmed the Court of Chancery's massive grant of custodial authority in that it did not consider less intrusive alternatives and ordered a sale despite shareholder objections—an unprecedented judicial act.[175] The court summarily accepted a custodial sale as the only means of appropriate relief, without considering that its equitable power—though significantly broad—may have *some limit*.[176]

167. *Id.* at 173.
168. *Id.* at 171 (citing Giuricich v. Emtrol Corp., 449 A.2d 232, 240 (Del. 1982)).
169. *Id.* at 183.
170. *Id.* at 184.
171. *Id.*
172. *Id.* at 186.
173. *See* discussion *infra* Part IV.A.
174. *See* discussion *infra* Part IV.A.
175. *See* discussion *infra* Part IV.B.
176. *See* discussion *infra* Part IV.B.

A. The Delaware Supreme Court Trivialized the Irreparable Harm Requirement of Section 226(a)(2)

Though Shawe and Elting stipulated to deadlock and satisfied the requirements of Section 226(a)(1), the Delaware Supreme Court affirmed the Court of Chancery's incorrect reasoning with respect to a custodial appointment under 226(a)(2) in dicta.[177] In doing so, it interpreted the irreparable harm requirement so as to encompass severely diminished employee morale, client skepticism, and failure to benefit from proposed acquisitions—notwithstanding the Company's profitability to date.[178] The court noted that, were the deadlock to persist, "the Company was likely to continue on the path of plummeting employee morale, key employee departures, customer uncertainty, damage to Company's public reputation and goodwill, and fundamental inability to grow the Company through acquisitions."[179] This, it held, was sufficient to demonstrate threatened and actual irreparable harm to the Company.[180] Section 226 jurisprudence and general principles of irreparable harm, however, suggest that this conclusion was flawed.

The irreparable harm requirement should not be satisfied when the corporation is in *no way* threatened with insolvency or loss of revenue.[181] In *Kleinberg*, for example, the Court of Chancery found the existence of threatened irreparable harm and noted that, unless the deadlock at issue came to an end, the company would "ha[ve] no chance of pursuing a new business plan and [would] become irretrievably insolvent."[182] Similarly, in *Hoban*, where deadlock amongst directors blocked a purportedly essential bank transition without which the company would "go under," the court found that irreparable harm existed, since "[s]ome change in financing arrangements [was] needed promptly if [the company was] to continue in business."[183] Conversely, in *Miller*, the court found that where "[t]he business of the corporation . . . [still] operate[d] reasonably well," irreparable

177. *Shawe,*157 A.3d at 162 (majority opinion).

178. *In re* Shawe & Elting LLC, No. 9661-CB, No. 9686-CB, No. 9700-CB, No. 10449-CB, 2015 Del. Ch. LEXIS 211, at *96–98 (Del. Ch. Aug. 13, 2015), *aff'd sub nom*. Shawe v. Elting, 157 A.3d 152 (Del. 2017).

179. *Shawe*, 157 A.3d at 162.

180. *Id.*

181. *See infra* notes 182–184 and accompanying text.

182. Kleinberg v. Aharon, No. 12719-VCL, 2017 Del. Ch. LEXIS 24, at *39 (Del. Ch. Feb. 13, 2017).

183. Hoban v. Dardanella Elec. Corp., No. 7615, 1984 Del. Ch. LEXIS 599, at *5–6 (Del. Ch. June 12, 1984).

harm was not demonstrated—in holding as it did, the court emphasized the profitability of the business.[184]

In support of its conclusion that irreparable corporate harm may include "harm to a corporation's reputation, goodwill, customer relationships, and employee morale," the Court of Chancery cited four cases[185]—all of which were insufficiently explained or were readily distinguishable from the facts of *In re Shawe & Elting LLC*. The first of the cases, *Kirpat, Inc. v. Delaware Alcoholic Beverage Control Commission*,[186] was cited in a parenthetical as "finding irreparable harm where the company would suffer 'loss of its customer base, and loss of its employees.'"[187] The company in *Kirpat*, however, would additionally "suffer the seizure of its inventory" and would consequently "lose its business" were the court to deny a stay pending appeal with respect to the revocation of the corporation's liquor license.[188] Thus, the loss of the *Kirpat* corporation's customer base and employees was less significant, as the seizure of the corporation's assets threatened insolvency and loss of revenue. The Court of Chancery failed to address this aspect of *Kirpat* and, instead, suggested that a failure to retain customers and employees, notwithstanding its effect on the company's profitability, is sufficient to establish irreparable harm.

The Court of Chancery then cited *Arkema, Inc. v. Dow Chemical Co.*[189] as "finding irreparable harm where an imminent threat to the company's goodwill and reputation existed."[190] This parenthetical, too, is lacking in holistic factual background. In *Arkema*, the corporation's business—the manufacture and sale of products containing a key chemical supplied by the defendant[191]—heavily depended on the company's reputation for reliabil-

184. Miller v. Miller, No. 2140-VCN, 2009 Del. Ch. LEXIS 16, at *9 (Del. Ch. Feb. 10, 2009).

185. *In re* Shawe & Elting LLC, No. 9661-CB, No. 9686-CB, No. 9700-CB, No. 10449-CB, 2015 Del. Ch. LEXIS 211, at *93 n.298 (Del. Ch. Aug. 13, 2015), *aff'd sub nom*. Shawe v. Elting, 157 A.3d 152 (Del. 2017) (citing Kirpat, Inc. v. Del. Alcoholic Beverage Comm'n, 741 A.2d 356, 358 (Del. 1998); Arkema Inc. v. Dow Chem. Co., No. 5479-VCP, 2010 Del. Ch. LEXIS 120, at *4 (Del. Ch. May 25, 2010); Penn Mart Supermarkets, Inc. v. New Castle Shopping LLC, No. 20405-NC, 2005 Del. Ch. LEXIS 199, at *15 (Del. Ch. Dec. 15, 2005); Shah v. Shah, No. 904(k), 1986 Del. Ch. LEXIS 467, at *2 (Del. Ch. Sept. 25, 1986)); *see supra* note 76. The Court of Chancery provided these four cases, and these four cases only, as support for its above the line proposition that irreparable corporate harm may include "harm to a corporation's reputation, goodwill, customer relationships, and employee morale." *In re Shawe & Elting LLC*, 2015 Del. Ch. LEXIS 211, at *93.

186. 741 A.2d 356 (Del. 1998).

187. *In re Shawe & Elting LLC*, 2015 Del. Ch. LEXIS 211, at *93 n.298 (citing *Kirpat*, 741 A.2d at 358).

188. *Kirpat*, 741 A.2d at 358.

189. No. 5479-VCP, 2010 Del. Ch. LEXIS 120 (Del. Ch. May 25, 2010).

190. *In re Shawe & Elting LLC*, 2015 Del. Ch. LEXIS 211, at *93 n.298 (citing *Arkema*, 2010 Del. Ch. LEXIS 120, at *4).

191. *Arkema*, 2010 Del. Ch. LEXIS 120, at *1.

ity.[192] This was so because the company's customers maintained quality control programs requiring them to "evaluate the reliability of their suppliers' supply chain."[193] To that end, the company was required to "compete continually to gain and retain its customers" and expressly marketed itself as more reliable than its competitors.[194] In the *Arkema* plaintiff's business, "reliability is essential when determining whether or not to choose a supplier," and harm to the company's reputation would directly result in the loss of "significant amounts of its business."[195] In fact, Arkema submitted several affidavits to show, *inter alia*, that the defendant's failure to supply the plaintiff with the chemical essential to its products would "cause Arkema to lose customers and business for an indefinite period going forward."[196] Thus, contrary to the Court of Chancery's analysis in *In re Shawe & Elting*, the *Arkema* decision does not stand for the proposition that damage to a company's reputation, without more, is sufficient to establish actual or threatened irreparable harm. The direct correlation between the company's reputation for reliability and the *profitability* of its business was of critical importance in the *Arkema* court's ultimate finding of threatened irreparable harm.

The third case cited by the Court of Chancery was *Penn Mart Supermarkets, Inc. v. New Castle Shopping LLC*,[197] which was described as "finding potential lost sales and lost customers sufficient to establish irreparable harm."[198] *Penn Mart* involved two lessees in a shopping center—one operating a supermarket ("Thriftway") and the other operating a discount store ("NWL").[199] The dispute arose from NWL's alleged violation of a lease covenant precluding it from selling certain perishable products and protecting Thriftway from competition.[200] The court found that the threat of irreparable harm existed where NWL's violation caused Thriftway to suffer "potential lost sales" and "loss of customers," thus entitling Thriftway to limited permanent injunctive relief.[201] The finding of irreparable harm in *Penn Mart* is completely consistent with the long-standing principle that irreparable harm can only be said to exist where loss of revenue or a decrease in profitability is imminent. It fails, however, to illustrate the Court of

192. *Id.* at *16.
193. *Id.*
194. *Id.* at *15–16.
195. *Id.* at *9, *17.
196. *Id.* at *16 (quoting Douglas Sharp Aff. p.54).
197. No. 20405-NC, 2005 Del. Ch. LEXIS 199 (Del. Ch. Dec. 15, 2005).
198. *In re Shawe & Elting LLC*, 2015 Del. Ch. LEXIS 211, at *93 n.298 (citing *Penn Mart*, 2005 Del. Ch. LEXIS 199, at *15).
199. 2005 Del. Ch. LEXIS 199, at *1.
200. *Id.* at *1, *4.
201. *Id.* at *69, *71.

Chancery's generalized above-the-line proposition that irreparable harm may include "harm to a corporation's reputation, goodwill, customer relationships, and employee morale."[202] At no point in *Penn Mart* does the court make such a determination.

The Court of Chancery finally cited *Shah v. Shah*[203] as "finding irreparable harm when disruptive management conflicts threatened employee retention."[204] In *Shah*, one of the part-owners of a local motel was accused of harassing the business's employees and interfering with the performance of their duties.[205] Entered into evidence were the affidavits of several employees expressing their intent to resign if the disruptive and "harassing" behavior of the part-owner towards them was not restrained.[206] Were the aggrieved employees to indeed resign, the court in *Shah* observed that "the [partnership's] operations [would] be severely impaired and may cease entirely," likely due to the motel's status as a small, service-oriented business.[207] The Court of Chancery in *In re Shawe & Elting* again failed to mention that the record in *Shah* indicated that that irreparable harm in the form of a complete *business shutdown* was imminent, absent court intervention. Thus, the partnership in *Shah* was indeed threatened with insolvency—mere lack of employee retention, without more, would have been unlikely to persuade the *Shah* court that the motel was threatened with irreparable harm.

The Delaware Supreme Court summarily and incorrectly affirmed the Court of Chancery's reasoning with respect to the irreparable harm requirement of Section 226(a)(2) without examining the sources cited in support of the Court of Chancery's expansive proposition. It concluded that "the Court of Chancery properly applied . . . settled principles of irreparable injury to evaluate the likelihood of threatened or actual irreparable injury to the Company's business."[208] This conclusion is flawed, since "settled principles of irreparable injury" have not traditionally been said to rest solely on diminished employee morale, client skepticism, and failure to benefit from proposed acquisitions notwithstanding the Company's profitability to date.[209]

202. *In re Shawe & Elting LLC*, 2015 Del. Ch. LEXIS 211, at *93.

203. No. 904(k), 1986 Del. Ch. LEXIS 467 (Del. Ch. Sept. 25, 1986).

204. *In re Shawe & Elting LLC*, 2015 Del. Ch. LEXIS 211, at *93 n.298 (citing *Shah*, 1986 Del. Ch. LEXIS 467, at *2).

205. *Shah*, 1986 Del. Ch. LEXIS 467, at *1.

206. *Id.* at *2, *6–7.

207. *Id.* at *7.

208. Shawe v. Elting, 157 A.3d 152, 161–62 (Del. 2017).

209. *In re Shawe & Elting LLC*, 2015 Del. Ch. LEXIS 211, at *96–98.

TransPerfect is a global behemoth that nets millions of dollars in annual income.[210] Tensions between Shawe and Elting peaked in 2012, but the Company's revenue two years later in 2014 exceeded an all-time high of $470 million.[211] Nothing in the record suggests that the Shawe and Elting feud jeopardized the Company's immense profitability, which was recognized expressly by Chancellor Bouchard in his opinion.[212] Despite the incessant corporate in-fighting, the Company "experienced profitable growth every year for over *two decades*."[213] In fact, after the Court of Chancery's decision issued, it was reported that the Company's revenue totaled $546 million in 2016—an "all-time record."[214] The Company had no debt.[215] Still, the Delaware Supreme Court concluded that TransPerfect was threatened with irreparable harm in the form of "harm to [its] reputation, goodwill, customer relationships, and employee morale."[216] In doing so, the court missed a significant nuance: the harms it describes are but the *means* by which irreparable corporate harm, as a separate and isolated consequence, ultimately manifests itself. Harms to a company's reputation, goodwill, customer relationships, and employee morale are certainly harms that could *theoretically* have an impact on the company's solvency or profitability; however, absent a grand scheme showing of an imminent and *direct* impact, they are insufficient of their own right to be deemed irreparable in nature. Incidental, typical, and expected harms that flow from corporate dissension should not be deemed sufficient to constitute irreparable harm, absent a demonstration of imminent insolvency or loss of revenue. The court's contrary conclusion—though made in dictum—sets a dangerous precedent and relaxes the threshold irreparable harm requirement, making it significantly easier to meet. In fact, Vice Chancellor Laster recently cited to this dictum in a subsequent decision, suggesting that the *In re Shawe & Elting LLC* court's proposition has become the new standard of analysis in the irreparable harm context.[217] Instead of exhausting intra-corporate reme-

210. *See supra* note 21 and accompanying text.

211. *See supra* note 20 and accompanying text.

212. *See In re Shawe & Elting LLC*, 2015 Del. Ch. LEXIS 211, at *91 ("It is true the Company has been highly profitable.").

213. *Id.* at *10 (emphasis added); *see id.* at *10 tbl.1 (charting the increase in the Company's profitability from 2008 when the Company's revenue totaled $199.1 million, to 2014 when the Company's revenue totaled $471.3 million).

214. *TransPerfect Annual Sales Reach All-Time High in 2016*, NASDAQ GLOBAL NEWSWIRE (Jan. 17, 2017), https://globenewswire.com/news-release/2017/01/17/906384/0/en/TransPerfect-Annual-Sales-Reach-All-Time-High-in-2016.html.

215. *Id.*

216. Shawe v. Elting, 157 A.3d 152, 161 (Del. 2017) (citing *In re Shawe & Elting LLC*, 2015 Del. Ch. LEXIS 211, at *93).

217. Kleinberg v. Aharon, No.12719-VCL, 2017 Del. Ch. LEXIS 24, at *37 (Del. Ch. Jan. 27, 2017) (quoting *In re* Shawe & Elting LLC, No. 9661-CB, No. 9686-CB, No. 9700-CB, No. 10449-CB, 2015 Del. Ch. LEXIS 211 (Del. Ch. Aug. 13, 2015)) ("The necessary harm also can

dies and attempting in good faith to resolve conflict outside the courtroom, it is likely directors looking to walk away from the business will petition the court for a more readily attainable custodianship remedy under Section 226(a)(2), using incidental effects of corporate dysfunction as the basis for their claim to irreparable harm.

Interestingly, the Court of Chancery and the Delaware Supreme Court both chose to entertain the 226(a)(2) argument *even though* custodianship was appropriate regardless under Section 226(a)(1).[218] Why would these courts—arguably the most sophisticated corporate tribunals in the country[219]—purposefully spend time discussing and validating an argument that was nonessential to the outcome of the case? The answer is simple: proportionality. The phrase "irreparable harm" carries massive weight in corporate jurisprudence. It appears in a multitude of equitable contexts, including that of the preliminary injunction,[220] that of the temporary restraining order,[221] and that of receivership.[222] In these circumstances, "irreparable harm" is pervasive legal language that signals a potential for injury so grievous that immediate equitable court intervention is required as a matter of justice.[223] The Court of Chancery and the Delaware Supreme Court seem to have intentionally framed the Shawe-Elting feud as a legally cognizable instance of irreparable harm so that a drastic equitable remedy would seem more justified. The courts deliberately weaved the "theme" of irreparable

result from damage to 'a corporation's reputation, goodwill, customer relationships, and employee morale.'"). Ultimately, as discussed *supra* in Part IV.A of this Note, the court in *Kleinberg* expressly found that insolvency was indeed imminent—it thus applied the correct irreparable harm standard to the facts before it, despite having cited the dictum in *In re Shawe & Elting LLC*. *See supra* note 182 and accompanying text.

218. *See supra* notes 69, 156 and accompanying text.

219. *See* Alana Semuels, *The Tiny State Whose Laws Affect Workers Everywhere*, ATLANTIC (Oct. 3, 2016), https://www.theatlantic.com/business/archive/2016/10/corporate-governance/502487/ ("[The Delaware Court of Chancery's] judges are some of the country's most renowned experts in business law.").

220. *See, e.g.*, *In re* Cogent, Inc. S'holder Litig., 7 A.3d 487, 497 (Del. Ch. 2010) (explaining that a preliminary injunction may only be granted if plaintiffs demonstrate that they would suffer irreparable injury absent relief).

221. *See* DEL. CH. R. 65(b) ("A temporary restraining order may be granted . . . only if . . . it clearly appears from specific facts . . . that immediate and irreparable injury, loss or damage will result to the applicant . . . .").

222. *See, e.g.*, Beal Bank v. Lucks, No. 14896, 1998 Del. Ch. LEXIS 203, at *13 (Del. Ch. Oct. 23, 1998) (explaining that the discretionary nature of the receivership remedy requires a consideration of the imminence of irreparable loss).

223. *See* DONALD J. WOLFE, JR. & MICHAEL A. PITTENGER, CORPORATE & COMMERCIAL PRACTICE IN THE DELAWARE COURT OF CHANCERY § 2.03 (2017) (explaining that "equitable jurisdiction may be invoked . . . only if the threat of the injury . . . is shown to be a real and continuing one"); *see also* Chateau Apartments Co. v. Wilmington, 391 A.2d 205, 208 (Del. 1978) ("For equity to assume jurisdiction . . . the danger to which the plaintiff is exposed must be a real one." (citing JOHN N. POMEROY & SPENCER W. SYMONS POMEROY'S EQUITY JURISPRUDENCE § 251 (5th ed 1995))).

harm into the fabric of their decisions to evince some degree of proportionality between the severity of Shawe and Elting's corporate dissension and the extremity of the ordered custodial sale. The courts' intentional in-depth, albeit unnecessary, analysis of Section 226(a)(2)'s irreparable harm requirement—despite its peripheral relevance to the case's outcome—persuades the conclusion that the courts may have been aware of how truly drastic the unprecedented remedy of an ordered custodial sale really was.

B. The Delaware Supreme Court Incorrectly Affirmed the Court of Chancery's Enormous and Unprecedented Grant of Power to the Appointed Custodian

In affirming the Court of Chancery's decision to appoint a custodian to sell the Company to a third party, the Delaware Supreme Court ignored the long-standing principle that "[t]he involvement of the Court of Chancery and its custodian in the corporation's business and affairs should be kept to a minimum and should be exercised only insofar as the goals of fairness and justice . . . require."[224] Section 226 jurisprudence has repeatedly spoken to the reluctance with which the Court of Chancery imposes the "intrusive" custodianship remedy[225] and to the principle that a custodian's authority should be as narrowly tailored as possible.[226] The Delaware Supreme Court should have reversed and recognized (1) that the Court of Chancery could have ordered a variety of less intrusive, incremental alternatives that would have kept its decision consistent with the aforementioned two principles, and (2) that the Court of Chancery's equitable power under Section 226 does not include the authority to order a custodial sale despite shareholder objections.

The court's decision could have been less intrusive in several ways. First, the court could have reversed with instructions to appoint a custodian, for a specified period of time, vested with (1) a tie-breaking vote; and (2) mediation powers—either as the courts in *Giuricich* and *Miller* did, where the custodians were vested with the power to break ties on *any issue* about which directors were deadlocked,[227] or as the court in *Bentas* did, where the custodian could only break the tie on issues "significant to managing the corporation's business and affairs."[228] This incremental remedy could have potentially tempered the animosity between Shawe and Elting, who may have been less inclined to act opportunistically knowing that their attempts

224. Giuricich v. Emtrol Corp., 449 A.2d 232, 240 (Del. 1982).

225. *See supra* notes 123–125 and accompanying text.

226. *See supra* notes 127–130 and accompanying text.

227. *See supra* notes 134, 138 and accompanying text.

228. Bentas v. Haseotes, 769 A.2d 70, 79 (Del. Ch. 2000); *see* text accompanying *supra* note 146.

would fail when the impartial third vote was cast. The Court of Chancery summarily rejected this option, however, observing that "it would enmesh an outsider and, by extension, the Court into matters of internal corporate governance for an extensive period of time."[229] Importantly, in its reasoning, the court nowhere considered the appointment of a provisional tie-breaking custodian with a *limited term* as a viable "first step" in the corporate healing process; instead, it fixed its conclusion on the *assumption* that the custodian's role would be indefinite.

Second, the court could have affirmed the decision to appoint a custodian, and could have ordered that both Elting and Shawe be given an opportunity to confer and submit proposals suggesting different scopes of custodial authority—just as the court did in *Miller*.[230] This may have incentivized cooperation among the parties whom, at that point, would have had to accept that custodianship was imminent and would have been more inclined to agree upon the precise corporate role the custodian would come to play. Third, the court could have forced a buy-out through a sealed bid process whereby either Shawe or Elting would have been given time to secure financing and would have been given the option to bid on the Company. A forced buy-out would have resolved the deadlock while simultaneously giving Shawe or Elting a chance to *maintain ownership* of the dorm room start-up that they built into a multi-million-dollar global giant.

Instead of implementing a less intrusive, incremental remedy in the first instance and reassessing its ruling in the event of further dispute or continued deadlock, the court accepted a one fell swoop excision in the form of a custodial sale as an appropriate remedy to eliminate the likelihood that dispute would recur altogether. In ruling as it did, the court essentially signaled that shareholders in closely held corporations would be wise to exhaust every last option before petitioning the court for relief—shareholders should be *so deadlocked* that they would be willing to risk a whole sale of their company. Though this may seem like a positive result, it may discourage deadlocked directors and shareholders from seeking intra-corporate recourse. For example, if an aggrieved fifty percent shareholder-director in a closely held corporation cannot secure her counterpart's cooperation in resolving the deadlock between them and cannot *compel* such cooperation because of the absence of a shareholders agreement, she now has two options. She can either (1) remain cemented in her ownership, thus allowing the deadlock to persist and thus running the risk of accelerating her company's demise; or (2) petition the court for a Section 226 custodial sale remedy. The second option gives the aggrieved shareholder an immediate exit—

229. *In re* Shawe & Elting LLC, No. 9661-CB, No. 9686-CB, No. 9700-CB, No. 10449-CB, 2015 Del. Ch. LEXIS 211, at *102 (Del. Ch. Aug. 13, 2015).

230. *See supra* note 141 and accompanying text.

armed with an arsenal of facts detailing her partner's lack of cooperation and opportunistic behavior, she now has the power to skip bona fide negotiation efforts and jump right to the option of equitable judicial intervention. And, that intervention may very well manifest itself in the form of a custodial sale—an ideal outcome, in this circumstance.

Additionally, the Delaware Supreme Court misinterpreted the bounds of the Court of Chancery's authority under Section 226, and improperly relied on distinguishable case law. As Justice Valihura explained in her dissent, there does not exist "a single case in the history of our Section 226 jurisprudence where a court has ordered a custodial sale of a company over a stockholder's objections."[231] In support of its proposition that "several sources confirm the Court of Chancery's broad authority under [Section 226], which includes ordering a sale," the majority cited several cases,[232] all of which are distinguishable from *Shawe v. Elting* in that they involved *consent by all of the stockholders* to a whole sale of the business. The majority expressly acknowledged this difference in a footnote, purporting to demonstrate the Court of Chancery's broad equitable discretion even though the examples it cited all "involve[d] actions where the parties eventually *agreed* the business should be liquidated or sold."[233] Where stockholder consent to a court ordered sale is present, the remedy is significantly less intrusive[234] and is thus consistent with the long-standing principle that the involvement of the Court of Chancery and its custodian should be kept to a minimum.[235] Absent stockholder consent, however, the court has never ordered the sale of a corporation to a third party—it thus erred in doing so in this instance. The Court of Chancery effectively forced divestiture of the Shawes' ownership interests without recognizing that the language and prior application of Section 226 failed to provide them with sufficient notice that a remedy as drastic as a whole sale of their company may occur.[236] As Justice Valihura pointed out in her dissent, Section 226 fails to provide express notice to stockholders that they may be subject to giving up their

231. Shawe v. Elting, 157 A.3d 152, 171 (Del. 2017) (Valihura, J., dissenting).

232. *Id.* at 163–64 n.36 (majority opinion) (citing Bentas v. Haseotes, No. 17223 NC, 2003 Del. Ch. LEXIS 24 (Del. Ch. Mar. 27, 2003); Fulk v. Wash. Serv. Assocs., No. 17747-NC, 2002 Del. Ch. LEXIS 78 (Del. Ch. June 21, 2002); *In re* Supreme Oil Co., Inc., No. 10618-VCL, 2015 Del. Ch. LEXIS 319 (Del. Ch. May 22, 2015); Brown v. Rosenberg, No. 833, 1981 Del. Ch. LEXIS 629 (Del. Ch. Dec. 17, 1981)); *see supra* note 163.

233. *Shawe*, 157 A.3d at 163–64 n.36 (emphasis added). Justice Valihura also distinguished these cases in her dissent, pointing to the presence of stockholder consent in each. *Id.* at 181 (Valihura, J., dissenting).

234. *Id.* at 183 (Valihura, J., dissenting).

235. Giuricich v. Emtrol Corp., 449 A.2d 232, 240 (Del. 1982).

236. *See supra* notes 166–167 and accompanying text.

shares over their objection;[237] it is thus unlikely that the Delaware General Assembly intended to permit the Court of Chancery to order the whole sale of a company to a third party, despite the absence of unanimous shareholder consent.[238]

V. CONCLUSION

In *Shawe v. Elting*, the Delaware Supreme Court improperly affirmed the Court of Chancery's unprecedented decision to order the custodial sale of a deadlocked corporation to a third party, despite stockholder objections.[239] In doing so, the court trivialized the irreparable harm requirement of Section 226(a)(2) and declined to holistically review the case law cited by the Court of Chancery in support of its proposition that irreparable harm may be deemed to encompass damage to "a corporation's reputation, goodwill, customer relationships, and employee morale."[240] The court also failed to recognize the unprecedented nature of a custodial sale absent stockholder consent and instead made a sweeping determination—without due consideration of less intrusive and incremental alternatives—that the Court of Chancery correctly concluded that whole sale was the only viable way to "excise" Shawe and Elting's dysfunction.[241] In February 2018, the Court of Chancery approved a $385 million cash purchase of the Company.[242] The purchaser was an entity owned and managed exclusively by

237. *Compare* DEL. CODE ANN. tit. 8, § 226 (1953) (containing no language that would provide shareholders with notice that their ownership interests may be affected absent their consent), *with* DEL. CODE ANN. tit. 8, § 251 (1953) (providing notice to stockholders objecting to a merger that their shares may be subject to divestiture or cancellation upon majority approval); DEL. CODE ANN. tit. 8, § 273 (1953) (providing notice to fifty-fifty shareholders that in the presence of threshold circumstances, their venture may be dissolved despite one shareholder's objection); *and* DEL. CODE ANN. tit. 8, § 303 (1953) (allowing a corporation filing for bankruptcy to, *inter alia*, "make any change in its . . . capital stock" or "be dissolved").

238. Shawe v. Elting, 157 A.3d 152, 173 (Del. 2017).

239. *See* discussion *supra* Part IV.

240. *See* discussion *supra* Part IV.A; *In re* Shawe & Elting LLC, No. 9661-CB, No. 9686-CB, No. 9700-CB, No. 10449-CB, 2015 Del. Ch. LEXIS 211, at *93 (Del. Ch. Aug. 13, 2015).

241. *See* discussion *supra* Part IV. B; *In re Shawe & Elting LLC*, 2015 Del. Ch. LEXIS 211, at *103.

242. *See In re* TransPerfect Global, Inc., No. 9700-CB, No. 10449-CB, at 33 (Del. Ch. Feb. 15, 2018). The Company's implied aggregate enterprise value was agreed upon and set at $770 million at the time of sale. *Id.* at 31.

none other than Phillip Shawe;[243] and like clockwork, Elting filed an appeal contesting the sale.[244] As one news outlet aptly put it: "The saga of TransPerfect will drag on a while longer."[245]

243. *Id.*; *see* Jeff Neiburg, *Chancery Court Approves Sale of TransPerfect*, DEL. ONLINE, Feb. 15, 2018, https://www.delawareonline.com/story/money/business/2018/02/15/chancery-court-approves-sale-transperfect/341189002/ (summarizing the details of the sale).

244. *Elting Reportedly Files Appeal on Chancery-led Sale of Company*, DEL. BUS. INSIDER, Feb. 26, 2018, https://delawarebusinessnow.com/2018/02/eating-reportedly-files-appeal-chancery-led-sale-company/.

245. *Id.*