

MEMORANDUM

TO: Members of the Opinion Standards Committee of the Business Law Section - January 10, 2013 Meeting

FROM: Robert W. Barron, Chair

DATE: January 9, 2013

RE: Special Report of the TriBar Opinion Committee: Duly Authorized Opinions on Preferred Stock – *The Business Lawyer*; Vol. 63, May 2008 – a Brief Outline for the January 10, 2013 Orlando Meeting

1. “Duly Authorized” Opinion means:

- a. “The shares are part of a class or series of shares that the Company has the authority to issue – i.e., are part of the authorized capital stock of the Company,
- b. When the shares are issued, the Company had a sufficient number of authorized shares of that class or series available for issuance,
- c. The proper procedural steps were taken to create the class or series of shares, including, if an amendment by the board of directors and/or the stockholders by the requisite vote of each class or series entitled to vote, as may be required by the applicable state corporation statute, and the filing of the amendment in the proper form with appropriate state officials,
- d. The Company’s charter contains all the substantive terms, for example, par value, number of authorized shares and preferences, required by the applicable state corporation statute to create the class or series of preferred stock; and
- e. The Company has the power under the applicable state corporation statute and its charter to create stock having rights, powers and preferences of the stock in question.”

2. Compliance with Statute and Charter

Regarding Item e - The starting point is the corporation statute. Typically, the opinion will address those issues which may be prohibited by, or violate, the corporation statute, such as, denial of voting rights, appraisal rights or inspection rights mandated by the statute. Economic terms of preferred stock, such as liquidation preferences or anti-dilution clauses, ordinarily do not violate the corporation statute, but they may violate the charter.

A “duly authorized” opinion encompasses the following statement “the rights, powers and preferences of the preferred stock set forth in the [charter] do not violate [the applicable corporate statute] or the [charter].”

3. Fiduciary Duties

The “duly authorized” opinion does not address whether the board of directors, in exercising its authority, discharged its fiduciary duties.

4. Remedies Opinion Issue for Preferred Stock Issuance

The “duly authorized” opinion does not cover a stockholder’s ability to enforce the provisions of the preferred stock.

- a. Opinion looks only to “power” of the Corporation under the corporation statute and charter to create the class of preferred stock in question.
- b. Opinion does not address whether the terms of the preferred stock will be given effect by the courts on a particular issue.
- c. Opinion does not cover compliance with disclosure requirements in state and federal securities laws in soliciting required shareholder approval of the charter amendment creating the preferred stock.
- d. An opinion on enforceability addresses contract law concepts (and includes the bankruptcy and equity exceptions) and preferred stock provisions are not governed by contract law but rather corporation law.
- e. One court has said – unlike a holder of debt – a holder of preferred stock does not have a “legally enforceable right to payment.” *Harbinger Capital Master Fund I, Ltd. v. Granite Broadcasting Corporation*, 906 A2d 218, 225 (Del. Ch. 2006).
- f. The concepts underlying an enforceability opinion “do not easily fit.”

5. Complex Issuances of Preferred Stock May Require Specific Exceptions in the Opinion

An unqualified opinion may not be possible in certain complex issuances and the opinion may include express exceptions to the “duly authorized” opinion. Examples of exceptions include:

- a. The charter establishes a procedure for declaring dividends that conflict with the corporation statute;
- b. The charter through a “drag along” provision conflicts with the corporation statute’s appraisal rights;
- c. The charter provides for a lower percentage vote for approval of certain matters than required by the corporation statute;
- d. The charter gives holders of a class of stock to designate members of a committee of the board but the corporation statute limits this right to the board; or
- e. The board pursuant to its blank check authority creates a non-voting class of stock but the charter only permits voting stock.

No exception is required in the opinion if the charter mandates redemption of the preferred stock through the corporation statute only permits redemption when the Company has sufficient legal funds available to effect the redemption. Many opinions include the phrase “to the extent funds are lawfully available therefor” – but TriBar states that this exception is not necessary – but advises that the opinion giver should point this limitation out to the opinion recipient. (Footnote 28).

6. Certain Problematic Provisions May Render the Entire Preferred Stock Invalid.

The entire preferred stock may not be valid if certain provisions are included in the preferred stock. The opinion giver may need to address in the opinion the possible effect of the provision on the validity of the preferred stock in its entirety.

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