NOTES

THE REGULATOR IN ROBES: EXAMINING THE SEC AND THE DELAWARE COURT OF CHANCERY'S PARALLEL DISCLOSURE REGIMES

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The Delaware Court of Chancery is a unique court that specializes in transactional jurisprudence. Due to Chancery's expertise in and exposure to corporate litigation, its decisions act as "rules" for most corporate actors. However, Chancery is not the only actor in the corporate law space, nor is it the most powerful. The SEC can—and has—intervened in state law by creating federal corporate law. In recent years, Chancery has issued many decisions in an area of corporate law—the disclosure of material information to shareholders—long associated with the SEC, with implications for actors determining their compliance with both "rulemaking" regimes.

This Note uses Chancery decisions addressing the disclosure of potential conflicts underlying a financial advisor's work in change-of-control transactions as a case study to highlight the substantive and procedural differences in SEC and Chancery disclosure "rules" and "rulemaking." This Note describes how Chancery has filled in gaps in SEC regulations on disclosing potential advisor conflicts. It also compares the SEC's and Chancery's rulemaking procedures to reveal two very different methods of regulating disclosure in change-of-control transactions.

While both the SEC and Chancery have comparative institutional advantages, there are costs to maintaining two independent disclosure "regulators" and increased harmonization would be valuable. This Note evaluates potential solutions to better reconcile the purpose of the SEC and the reality of Chancery's active involvement in determining disclosure obligations. It concludes that the SEC should codify Chancery's decisions, subjecting them to a formal rulemaking process.

INTRODUCTION

Over the past century, the Delaware Court of Chancery ("Chancery") has developed unrivaled expertise in adjudicating corporate disputes.[1] Due to Delaware's role as the premier state for incor-

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1. See Stephen M. Bainbridge, The Business Judgment Rule as Abstention Doctrine, 57 Vand. L. Rev. 83, 121 (2004) ("Unlike other courts, which face corporate cases only

porations, most corporations are subject to Delaware common law.[2] As a result, Chancery's decisions often act as "rules" for dealmakers nationwide.[3]

Chancery, however, is not the only actor in the corporate law space, nor is it the most powerful.[4] The federal government, whether through Congress or the Securities and Exchange Commission (SEC), can—and has—intervened in state law by creating federal corporate law.[5] The SEC was created to promulgate federal rules while leaving space for states to regulate corporate affairs.[6] Indeed, SEC rulemaking is often supplemented by Delaware common law.[7]

Many have argued in support of either Chancery or SEC primacy in the creation of corporate law. Proponents of Chancery highlight the unique attributes of the court to argue that its rulings combine the flexibility and efficiency afforded by a court of equity[8] with the predictability more characteristic of rules promulgated by a regulatory agency.[9] Some

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episodically, such cases make up a very high percentage of the Delaware chancellors' docket. The frequency . . . provides a strong incentive for Delaware's chancellors to master both doctrine and the business environment in which the doctrine works."); see also D. Gordon Smith, Chancellor Allen and the Fundamental Question, 21 Seattle U. L. Rev. 577, 579 (1998) (referring to Chancery as "nation's guardians of corporate law").

2. See, e.g., Faith Stevelman, Regulatory Competition, Choice of Forum, and Delaware's Stake in Corporate Law, 34 Del. J. Corp. L. 57, 66 (2009) ("Among the fifty states, Delaware has visibly succeeded in claiming the number one spot in attracting and retaining incorporations."); see also Lucian Arye Bebchuk & Assaf Hamdani, Vigorous Race or Leisurely Walk: Reconsidering the Competition over Corporate Charters, 112 Yale L.J. 553, 554 n.3 (2002) ("Delaware is the state of incorporation for fifty-seven percent of U.S. public companies and for fifty-nine percent of Fortune 500 companies.").

3. Bebchuk & Hamdani, supra note 2, at 554 ("Delaware . . . plays a central role in setting corporate governance rules for the nation's publicly traded companies.").

4. See, e.g., Stevelman, supra note 2, at 60 ("Congress could always preempt corporate law for public companies based on its authority under the Commerce Clause.").

5. See infra Part I.A (describing SEC disclosure rules); infra Part II.A (describing disclosure rules rooted in Securities Exchange Act of 1934).

6. See infra text accompanying notes 115–120 (describing purpose of SEC and space left for state regulation).

7. See infra Part I.B (describing Chancery's gap-filling of broad SEC rules on disclosure of financial advisor conflicts).

8. See, e.g., Sean J. Griffith & Myron T. Steele, On Corporate Law Federalism: Threatening the Thaumatrope, 61 Bus. Law. 1, 8–13 (2005) (arguing state regulation of corporate governance is superior because federal rules are either over- or underinclusive and because inherent uncertainty of courts incentivizes more explicit contracting for unknown future states of world); E. Norman Veasey with Christine T. Di Guglielmo, What Happened in Delaware Corporate Law and Governance from 1992–2004? A Retrospective on Some Key Developments, 153 U. Pa. L. Rev. 1399, 1413 (2005) (referring to corporate law as "both inherently and usefully indeterminate, because it allows business practices and expectations to evolve, and enables courts to review compliance with those evolving practices and expectations").

9. See Griffith & Steele, supra note 8, at 11 (arguing Delaware judges are able to mitigate reactive nature of courts, and suggesting "[t]hrough the concise and limited use of dicta, state courts can act prospectively in much the same way as regulators"); Roberta

scholars have gone as far as to suggest that Chancery is able to "announce forward looking rules" and develop procedures to receive and consider commentary, such that "the Court has largely captured the substantive and procedural benefits of notice-and-comment rulemaking" that are obtained through regulatory agencies.[10]

However, the literature is also rife with those calling for further federal intervention in corporate law.[11] Many point to the SEC's statutorily mandated rulemaking process as a necessary element of a predictable and representative body of corporate law.[12] Some scholars have highlighted the uncertainty inherent in corporate law arising from specific facts before a court.[13] Others have suggested that Chancery repre-

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Romano, Law as a Product: Some Pieces of the Incorporation Puzzle, 1 J.L. Econ. & Org. 225, 280 (1985) (noting factors such as Chancery's greater exposure to and experience with corporate law cases, its use of unpublished court opinions, and its solicitation of views of corporate bar "afford firms greater predictability of the legal outcomes of their decisions, facilitating planning and reducing the costs of doing business"); Veasey with Di Guglielmo, supra note 8, at 1505 (arguing specialized experience and competency of Delaware judges creates legal predictability and noting federal intervention could mean "degree of reasonable stability we have come to expect from Delaware judge-made law and legislation could be lost").

10. William Savitt, The Genius of the Modern Chancery System, 2012 Colum. Bus. L. Rev. 570, 571, 587; see also Jill E. Fisch, The Peculiar Role of the Delaware Courts in the Competition for Corporate Charters, 68 U. Cin. L. Rev. 1061, 1085–88 (2000) [hereinafter Fisch, Peculiar Role] (arguing Chancery's responsiveness, flexibility, and forward-looking jurisprudence allow Chancery to approximate administrative rulemaking).

11. See, e.g., Bebchuk & Hamdani, supra note 2, at 608–15 (making "case for a federal rule that would govern reincorporation decisions and for a federal incorporation option"); William L. Cary, Federalism and Corporate Law: Reflections upon Delaware, 83 Yale L.J. 663, 701–03 (1974) (arguing for "federal standards of corporate responsibility"); cf., e.g., Joel Seligman, The Case for Federal Minimum Corporate Law Standards, 49 Md. L. Rev. 947, 971–74 (1990) (arguing state law does not hold corporate managers sufficiently accountable).

12. The SEC has been favored by many as a corporate regulator due to its formalized rulemaking process. See, e.g., Steven M. Davidoff, The SEC and the Failure of Federal Takeover Regulation, 34 Fla. St. U. L. Rev. 211, 266 (2007) [hereinafter Davidoff, Takeover Regulation] ("[R]ule-based regulation is produced through a responsive deliberative process that involves a comment period and public input. It is consequently more nuanced, targeted, and globally consistent than regulation issued on a case-by-case basis."); Robert A. Prentice, The Inevitability of a Strong SEC, 91 Cornell L. Rev. 775, 801–02 (2006) (noting, as compared to individuals making decisions, SEC "publishes proposed rules, entertains a lengthy comment period, examines the comments, and responds to them," and "[i]f the SEC proposes a controversial rule, advocates, opponents, investors, securities professionals, academics, and others lodge thousands of comments," often leading to revision of rule).

13. For the argument that Delaware's case-by-case decisions lead to uncertainty, see William J. Carney & George B. Shepherd, The Mystery of Delaware Law's Continuing Success, 2009 U. Ill. L. Rev. 1, 11–17, 36–39, which discusses how different rules stemming from cases with similar fact patterns lead to indeterminacy for corporate planners. Carney and Shepherd also discuss how the Delaware courts are constrained, like all courts, by stare decisis, and argue that the requirement to adhere to and distinguish precedent leaves the current law in "disarray," increasing inefficiency and costs for actors. Id. at 69–

sents a narrow set of interests, and thus is unqualified to "regulate" corporate decisions that affect a broad set of constituencies.[14]

Testing these opposing views of Chancery's and SEC's competencies as "regulators" would be very difficult. This Note does not judge the superiority of administrative and legislative rulemaking or judge-made law for creating corporate law. However, in recent years, Chancery has issued many decisions in an area of corporate law—the disclosure of material information to shareholders—long associated with the SEC, with implications for actors determining their compliance with both corporate "rulemaking" regimes.

This Note focuses on Chancery's decisions regarding the disclosure of potential conflicts underlying a financial advisor's work in change-of-control transactions. Chancery has required affirmative disclosure in many instances when directors seek some form of shareholder action.[15] The Delaware statute governing corporate law provides minimum disclosure requirements, but Chancery has derived—from state law fiduciary duties—affirmative obligations for corporations to disclose material[16] facts to their shareholders.[17] In particular, Chancery has increased its scrutiny of the work of financial advisors in recent years, and claims about financial advisor-related disclosure are frequently litigated, providing a significant amount of case law.[18] The law on disclosure of financial advisor conflicts thus serves as an effective case study of the regulatory dynamic between the SEC and Chancery.[19]

72; see also Ehud Kamar, A Regulatory Competition Theory of Indeterminacy in Corporate Law, 98 Colum. L. Rev. 1908, 1912–23 (1998) (suggesting Delaware corporate law's "legal indeterminacy" helps create "suboptimal equilibrium").

14. See infra notes 158–161 and accompanying text (describing scholarship on interests represented in Delaware).

15. See infra Part I.B (discussing Chancery rulings on disclosure issues).

16. The standard for materiality is the same in Delaware as that announced by the Supreme Court in TSC Industries, Inc. v. Northway, Inc., 426 U.S. 438 (1976): "An omitted fact is material if there is a substantial likelihood that a reasonable shareholder would consider it important in deciding how to vote" or if there is "a substantial likelihood that . . . disclosure of the omitted fact would have been viewed by the reasonable investor as having significantly altered the 'total mix' of information made available." Rosenblatt v. Getty Oil Co., 493 A.2d 929, 944 (Del. 1985) (quoting *TSC Indus., Inc.*, 426 U.S. at 449).

17. See Robert B. Thompson, Delaware's Disclosure: Moving the Line of Federal-State Corporate Regulation, 2009 U. Ill. L. Rev. 167, 181 [hereinafter Thompson, Delaware's Disclosure] (noting Delaware statute requires little in regards to affirmative disclosure and such obligations stem from state-law-based fiduciary duty developed by Chancery).

18. See infra Part I.B (discussing Chancery rulings on disclosure of financial advisor conflicts).

19. However, this is just one area of disclosure law where Chancery has provided a significant amount of case law in recent years. Other disclosure obligations deserve further study because each specific area of the law may highlight different aspects of the interplay between SEC and Chancery rules. For example, Chancery has ruled quite frequently on the extent of disclosure necessary for the analyses underlying fairness opinions provided

Despite Chancery's increasing recognition of disclosure obligations, since its creation in the Securities Exchange Act of 1934 ("Exchange Act"), the SEC has used disclosure as its main regulatory tool.[20] Congress tasked the SEC with creating disclosure rules for corporate actors,[21] so presumably Congress hoped to obtain the benefits of a formal rulemaking regime in producing disclosure regulations. The manner in which Chancery has filled the gaps of the SEC disclosure regime for the work of financial advisors suggests it is increasingly acting as a principal determinant of disclosure obligations.[22]

This Note highlights the substantive and procedural differences between the Chancery and SEC disclosure regimes and argues that the current status quo of two wholly independent disclosure "regulators" is suboptimal and contrary to the purpose of the Exchange Act. Part I compares the substantive differences in the SEC's and Chancery's approaches to disclosure, focusing on the example of financial advisor conflicts. The SEC creates broad disclosure rules that are supplemented by its staff's interpretations, while Chancery uses dicta to provide guidance to corporate actors but often decides disclosure issues based on the totality of the facts.

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by financial advisors in support of a proposed transaction. See, e.g., Maric Capital Master Fund, Ltd. v. Plato Learning, Inc., 11 A.3d 1175, 1176–78 (Del. Ch. 2010) (concluding proxy statement was materially deficient because it did not disclose free cash flow estimates and discount rates relied upon by financial advisors); In re Netsmart Techs., Inc. S'holders Litig., 924 A.2d 171, 201–04 (Del. Ch. 2007) (holding proxy statement deficient when lacking projections underlying financial advisor's fairness opinion); In re Pure Res., Inc., S'holders Litig., 808 A.2d 421, 448–50 (Del. Ch. 2002) (requiring disclosure of "fair summary of the substantive work performed by the investment bankers").

20. See, e.g., Stephen M. Bainbridge, Mandatory Disclosure: A Behavioral Analysis, 68 U. Cin. L. Rev. 1023, 1023 (2000) ("Mandatory disclosure is a—if not *the*—defining characteristic of U.S. securities regulation."); Thompson, Delaware's Disclosure, supra note 17, at 167 (noting disclosure is "primary domain of the federal regulators").

21. See, e.g., Affiliated Ute Citizens of Utah v. United States, 406 U.S. 128, 151 (1972) ("The Court has said that the 1934 Act and its companion legislative enactments embrace a 'fundamental purpose . . . to substitute a philosophy of full disclosure for the philosophy of *caveat emptor* and thus to achieve a high standard of business ethics in the securities industry.'" (quoting SEC v. Capital Gains Research Bureau, Inc., 375 U.S. 180, 186 (1963))); see also Bus. Roundtable v. SEC, 905 F.2d 406, 411 (D.C. Cir. 1990) ("In 1934 Congress acted on the premise that shareholder voting could work, so long as investors secured enough information and, perhaps, the benefit of other procedural protections. It did not seek to regulate the stockholders' choices."); Lloyd L. Drury, III, Private Equity and the Heightened Fiduciary Duty of Disclosure, 6 N.Y.U. J.L. & Bus. 33, 70 (2009) ("[D]isclosure is squarely within the ambit of the SEC and only an ancillary concern of state fiduciary law."); Thompson, Delaware's Disclosure, supra note 17, at 189 (noting recurring judicial statements reaffirming "purpose of the 1934 Act to require disclosure so as to permit informed shareholder action").

22. See Thompson, Delaware's Disclosure, supra note 17, at 187 ("[T]he SEC provides the details of mandatory disclosure, but the Delaware courts are the front line in the application of those requirements to specific corporate transactions.").

Part II examines the characteristics and implications of the two different rulemakers. It discusses the SEC's mandate to create disclosure rules to protect investors and outlines the procedural differences between SEC and Chancery rulemaking. Part II suggests that the differing substantive and procedural approaches to the same set of disclosure obligations increases uncertainty and denies corporate law the potential benefits of SEC and Chancery collaboration. Part III evaluates potential solutions to reconcile the purpose of the SEC and the reality of Chancery's active involvement in determining disclosure obligations. It suggests that the SEC confirm and codify Delaware's rules, subjecting them to a formal rulemaking process.

I. Disclosure Rules

In recent years, Chancery has been particularly active in cases involving disclosure issues in various change-of-control transactions.[23] Change-of-control transactions—where control of the corporation is acquired by another entity[24]—generally require shareholder approval.[25] Requiring

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23. In a series of rulings in the past decade, Chancery has increasingly noted the importance of adequate disclosure in various types of change-of-control transactions, including those transactions—such as management buyouts (MBOs) and freezeout transactions—that are especially prone to conflicts of interest. In these types of acquisitions, officers or controlling shareholders are on both sides of a transaction and are therefore less incentivized to maximize the target corporation's sale price.

For conflicts of interest inherent in MBOs, see, for example, Mills Acquisition Co. v. Macmillan, Inc., 559 A.2d 1261, 1279 (Del. 1988), which noted that management, as a participant in a proposed leveraged buyout, had a significant self-interest in ensuring the success of that bid. See also In re Formica Corp. S'holders Litig., No. 10598, 1989 WL 25812, at *10 (Del. Ch. Mar. 22, 1989) (noting inherent conflict of interest when "[m]anagement's personal motivation as a potential buyer is to pay as little as possible" and "[m]anagement's duty as a fiduciary is to obtain the highest available value for the stockholders"); Benjamin J. Stein, Shooting Fish in a Barrel: Why Management Always Makes a Bundle in an LBO, Barron's Nat'l Bus. & Fin. Wkly., Jan. 12, 1987, at 6, 20 (asserting combination of management's control position and exposure to material nonpublic information allows management to appropriate private gains at expense of shareholders).

For conflicts of interest inherent in freezeout transactions, see, for example, *In re Pure Res.*, 808 A.2d at 442–43 (noting informational and timing advantages possessed by controller in both merger and tender offer freezeout transactions); Robert Charles Clark, Corporate Law 507–08 (1986) (noting potential for investor harm inherent in freezeout transactions because stock prices may not reflect value of totality of information available to controller); Guhan Subramanian, Fixing Freezeouts, 115 Yale L.J. 2, 31–34 (2005) (noting tender offer freezeouts are susceptible to opportunistic behavior by controller, who can either time tender offer strategically to capture market price of target lower than its intrinsic value or engage in value-reducing behavior to generate lower price).

24. E.g., Paramount Commc'ns Inc. v. QVC Network Inc., 637 A.2d 34, 43 (Del. 1994) (describing "change of control transaction" as sale of control by board to another entity).

25. See, e.g., Blake Rohrbacher & John Mark Zeberkiewicz, Fair Summary: Delaware's Framework for Disclosing Fairness Opinions, 63 Bus. Law. 881, 882 (2008)

the board of directors to disclose all material information in its possession when seeking shareholder approval for these transactions is one way of mitigating the risk of conflicted parties undermining shareholder value.[26]

The advice relied upon by the board of directors in making its recommendation on a merger or tender offer is likely to be of major importance to shareholders deciding whether to vote for or against a proposed deal.[27] Most boards will hire a financial advisor, usually an investment bank, to advise on the fairness of a proposed transaction. The opinion of the financial advisor will generally be presented to shareholders in the form of a fairness opinion.[28] While the fairness opinion is the "bottom-line conclusion" of the advisor, the substantive analyses underlying the opinion are also of interest to shareholders considering voting for a merger or agreeing to tender their shares.[29]

Given the importance of the financial advisor's analyses, shareholders are interested in the advisor's potential conflicts of interest.[30] Such conflicts may include the investment bank or its employees' financial interest in a particular deal, the bank's previous business relationships with either side to a transaction, and the structure of the bank's fee arrangement.[31] Part I.A discusses the SEC's rules on disclosing the financial advisor's potential conflicts of interest and how they have generally been interpreted. Part I.B describes how Chancery has filled gaps in the

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[hereinafter Rohrbacher & Zeberkiewicz, Fair Summary] ("[W]hen a target board adopts a resolution approving a merger agreement, the stockholders must decide whether to approve the merger . . . . When a tender offeror makes an offer to the stockholders of a public company, the target board must state its position on the offer . . . for the stockholders' information." (footnote omitted)); see also 17 C.F.R. § 240.14e-2(a) (2012) (requiring target company to disclose to shareholders its recommendation, neutrality, or inability to make recommendation on tender offer within ten business days of proposal).

26. See, e.g., TSC Indus., Inc. v. Northway, Inc., 426 U.S. 438, 448 (1976) (noting purpose of SEC tender offer regulation is to "ensure disclosures by corporate management in order to enable the shareholders to make an informed choice").

27. See infra Part I.A (discussing SEC regulations requiring disclosure of summary of financial advisor's work in evaluating fairness of transaction); infra Part I.B (discussing Delaware's approach to disclosure of potential conflicts of interest for advisors).

28. Fairness opinions are "provided by an outside advisor, usually, though not necessarily, an investment bank" and are rendered to advise the board and shareholders that a "transaction meets a threshold level of fairness from a financial perspective." Steven M. Davidoff, Fairness Opinions, 55 Am. U. L. Rev. 1557, 1558 (2006) [hereinafter Davidoff, Fairness Opinions].

29. See In re Pure Res., Inc., S'holders Litig., 808 A.2d 421, 449 (Del. Ch. 2002) ("[I]nvestment bankers' analyses . . . usually address the most important issue to stockholders—the sufficiency of the consideration being offered to them for their shares in a merger or tender offer.").

30. See, e.g., La. Mun. Police Employees' Ret. Sys. v. Crawford, 918 A.2d 1172, 1191 (Del. Ch. 2007) ("Knowledge of such financial incentives on the part of the bankers is material to shareholder deliberations.").

31. See infra Part I.B (describing Chancery rulings on financial advisor conflicts).

SEC disclosure rules in a series of opinions discussing when such conflicts must be disclosed.

A. *SEC Regulations on Disclosure of Financial Advisor's Potential Conflicts of Interest*

Disclosure obligations as to a financial advisor's conflicts are generally litigated in the context of shareholders voting on a change-of-control transaction, whether such a transaction is characterized as a going-private transaction, merger, or tender offer. The SEC promulgates disclosure rules for each type of transaction.[32]

For going-private transactions and mergers, the SEC's disclosure rules require the filing company to state whether it has received a fairness opinion from an advisor.[33] SEC regulations require disclosure of "any material relationship that existed during the past two years or is mutually understood to be contemplated and any compensation received or to be received as a result of the relationship between" the advisor and the subject company and its affiliates.[34] It is important to note that the requirement applies only to the advisor and the "company (and its affiliates) for which the [advisor] is rendering the fairness opinion," and not to the company on the other side of the transaction.[35] As stated, the rule requires disclosure of any material relationship between the bank rendering the fairness opinion and the subject company in the past two years and a description of the compensation stemming from that relationship. While the disclosure must indicate whether some of the compensation is contingent on the completion of the transaction, the disclosure need not quantify the amount of compensation so contingent.

The contours of SEC rules are often shaped by the SEC staff, who provide guidance in the form of various interpretations, including "no action letters"[36] and generally applicable interpretive guidelines.[37] These

32. Securities Exchange Act of 1934, 15 U.S.C. §§ 78a–78pp (2012).

33. Item 1015, 17 C.F.R. § 229.1015(a) (2013) (requiring filer to disclose receipt of "[a]ny report, opinion or appraisal relating to the consideration or the fairness of the consideration to be offered to security holders or the fairness of the transaction to the issuer or affiliate or to security holders who are not affiliates").

34. § 229.1015(b)(4).

35. Self-Regulatory Organizations: National Association of Securities Dealers, Inc., Exchange Act Release No. 34-53598, 71 Fed. Reg. 18,395, 18,397 (proposed Apr. 11, 2006).

36. No action letters are responses by SEC staff to counsel which indicate that the agency will not recommend an enforcement action against the counsel's client if the client "proceeds along the lines indicated in the letter." John C. Coffee, Jr. & Hillary A. Sale, Securities Regulation 60 (12th ed. 2012). They are not binding on the SEC or private parties, but are made generally available and are viewed as guidance. Id. at 60–61.

37. See Staff Interpretations, Sec. & Exch. Comm'n, http://www.sec.gov/interps.s html (on file with the *Columbia Law Review*) (last visited Sept. 29, 2013) ("These staff interpretations provide guidance to those who must comply with the federal securities laws.").

interpretations provide guidance to filing companies that must comply with federal securities laws, but are not legally binding because they represent the views of the staff and not the SEC itself.[38] SEC interpretive guidelines have failed to go much further than SEC rules in regulating disclosure of financial advisor conflicts and state that the filing company need only disclose "whether . . . any of the compensation is contingent upon the successful completion of the transaction" and the amount of the total fee.[39]

The SEC staff also shapes disclosure obligations through comment letters written in response to parties filing disclosure documents.[40] The staff may respond to a filer's disclosure by requesting that the filer provide supplemental information, which may lead to several rounds of back and forth between the filer and staff before they resolve the issue.[41] The letters are publicly available on the SEC's website to serve as guidance for subsequent filers considering the amount of information to disclose.[42] However, the staff often takes positions based on the specific context of a filing and focuses on each subject company's particular situation.[43] Just like the interpretive guidelines, the comment letters reflect the views of the SEC staff and not the Commission itself, and thus are not legally binding.[44] Indeed, the Commission may overrule staff interpretation by taking a position inconsistent with previous review.[45] The SEC staff may also change its views on an issue and cease to follow earlier positions.[46] The fact-specific and variable nature of staff positions may undermine the guidance function of some of the published comment letters.

In the going-private context, SEC staff review of financial advisor conflicts has traditionally been inconsistent—"[w]hile the staff has some-

38. Id.; see also Coffee & Sale, supra note 36, at 60 ("[N]o-action letters are not binding on the Commission.").

39. Going Private Transactions, Exchange Act Rule 13e-3 and Schedule 13E-3, Sec. & Exch. Comm'n, http://www.sec.gov/divisions/corpfin/guidance/13e-3-interps.htm (on file with the *Columbia Law Review*) (last updated Jan. 26, 2009).

40. See Comment Letters, Sec. & Exch. Comm'n, http://www.sec.gov/answers/commentletters.htm (on file with the *Columbia Law Review*) (last modified Apr. 18, 2011) (explaining SEC comment letters).

41. Id.

42. See id. (explaining SEC made all correspondence related to filings after August 1, 2004, public).

43. See id. ("The staff's comments are in response to a company's disclosure and other public information and are based on the staff's understanding of that company's facts and circumstances.").

44. See id. (noting staff letters are not binding on Commission).

45. E.g., Coffee & Sale, supra note 36, at 60–61 (noting Commission does "from time to time . . . overrule the staff, usually prospectively, and take[] a position inconsistent with the staff's interpretation").

46. See N.Y.C. Employees' Ret. Sys. v. SEC, 45 F.3d 7, 14 (2d Cir. 1995) (noting SEC is not required to follow notice-and-comment procedures of Administrative Procedure Act in issuing interpretations reversing long-established staff position).

times required full disclosure of relationship details as well as monetary and other compensation provided," until recently the staff accepted descriptive boilerplate responses that "did not detail the true nature and extent of the investment bank and corporate relationship, past and present, nor the amount of compensation received by the investment bank."[47] Additionally, the SEC staff does not review every disclosure document before shareholders vote on a merger proposal, so the SEC filing that shareholders receive may retain boilerplate language.[48]

In the merger context, the regulation of the disclosure of "material relationships" between financial advisors and filers has been lax as well; the SEC often accepts boilerplate disclosures describing fees and past relationships as "customary."[49] Just as in the going-private context, the SEC staff inconsistently requests more information about the contingent nature and amount of fees, although recent proxy statements often disclose the contingent nature and amount of the advisor fees.[50]

In the tender offer context, SEC regulations require the company whose outstanding securities are being tendered to either make a recommendation to shareholders to accept or reject the offer or explain why it is remaining neutral.[51] The board of the target company will often hire an advisor to evaluate the fairness of a proposed tender offer. Disclosure of the financial advisor's potential conflicts is not required by SEC regulations; disclosure in tender offer situations is required only if

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47. Davidoff, Fairness Opinions, supra note 28, at 1592–93.

48. See Peter J. Rooney, Mergers & Acquisitions Alert: Delaware Court Enjoins Pending $3.1 Billion Merger Due to Inadequate Disclosure Regarding Financial Advisor's Fees and CEO Employment Arrangements, Orrick, Herrington & Sutcliffe LLP, at 3 (Mar. 10, 2011), http://www.orrick.com/fileupload/3430.pdf (on file with the *Columbia Law Review*) ("[I]t is . . . common . . . for parties to submit materials . . . [disclosing] that 'customary fees' will be paid and . . . 'substantial portion' of such fees are contingent upon . . . closing of the transaction, in hopes that, in the absence of SEC staff review, such a vague description can be retained in . . . final disclosure documents.").

49. Davidoff, Fairness Opinions, supra note 28, at 1593–94.

50. See, e.g., Sun Microsystems, Inc., SEC Response Letter (June 1, 2009), available at http://sec.gov/Archives/edgar/data/709519/000119312509122778/filename1.htm (on file with the *Columbia Law Review*) (responding to request for details on contingent amount of bank fees); Sirius Satellite Radio Inc., SEC Response Letter (Oct. 1, 2007), available at http://www.sec.gov/Archives/edgar/data/908937/000095012307013261/filename20.htm (on file with the *Columbia Law Review*) (responding to request for comment on contingency fees and potential risk factor disclosure issues); Host Marriott Corp., SEC Response Letter (Feb. 7, 2006), available at http://www.sec.gov/Archives/edgar/data/1070750/000119312506021852/filename15.htm (on file with the *Columbia Law Review*) (responding to request for disclosure of potential conflict of interest related to advisor fees).

51. Item 4, Schedule 14D-9, 17 C.F.R. § 240.14d-101 (2012) (requiring subject company to "[f]urnish the information required by Item 1012(a) through (c) of Regulation M-A"). Item 1012 of Regulation M-A requires filers to state the nature of their recommendation and "the reasons for [their] position (including the inability to take a position)." Id. § 229.1012(a)–(b).

the staff requests it.[52] Again, the extent of disclosure is based on fact-specific and variable staff positions.[53] As such, SEC disclosure requirements for the material relationships between the financial advisor and the parties are even less clear in the tender offer context than in the going-private and merger contexts.

B. *Delaware Courts Fill the Gaps in SEC Disclosure Rules*

The SEC and Chancery have promoted two different approaches to the disclosure of financial advisor conflicts. The SEC has created very broad disclosure rules, with the extent of particular disclosure obligations developed through nonbinding staff interpretations. Chancery has elaborated specific disclosure obligations for potential conflicts of interest in a succession of recent cases as the independence of the financial advisor has garnered intensified scrutiny.[54] Chancery has gone further than the SEC, highlighting certain areas of concern both in its holdings and dicta. Proponents of Chancery's primacy in corporate law point to the court's ability to use dicta to provide prospective guidance for future dealmakers while ruling on the merits of the case at hand.[55] Some scholars have even gone so far as to compare Chancery dicta to enforcement guidelines or regulatory interpretations that are used to influence an entire set of future actors without binding the parties before the court.[56] In recent years, Chancery has, through innovative use of dicta, provided guidance on the disclosure of financial advisor conflicts. However, the fact-specific nature of Chancery decisions differentiates them from the broad, prospective rules typically generated by regulatory agencies.[57]

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52. Item 1015 of Regulation M-A, requiring disclosure of "material relationships," id. § 229.1015(b)(4), is not incorporated into Schedule 14D-9. Id. § 240.14d-101.

53. See supra notes 36–46 and accompanying text (describing fact-specific and nonbinding nature of SEC staff review).

54. David P. Simonetti Rollover IRA v. Margolis, No. 3694-VCN, 2008 WL 5048692, at *8 (Del. Ch. June 27, 2008) (noting because of fairness opinion's importance as "process-based underpinning[] of a board's recommendation of a transaction to its stockholders and . . . for the stockholders' decisions on the appropriateness of the transaction[,] . . . it is imperative for the stockholders to be able to understand what factors might influence the financial advisor's analytical efforts").

55. See Savitt, supra note 10, at 590 ("[R]ecourse to dictum allows Chancery to prospectively regulate fiduciary conduct, without requiring the litigants before it to bear the cost (through retrospective application) of prospective rulemaking."); Myron T. Steele & J.W. Verret, Delaware's Guidance: Ensuring Equity for the Modern Witenagemot, 2 Va. L. & Bus. Rev. 189, 207 (2007) ("The Delaware courts recognize the need to wait for a live controversy to resolve an issue definitively, but . . . also recognize that . . . they [may] . . . use the attention paid to a published opinion to offer guidance on uncertain but vital areas of corporate law.").

56. Savitt, supra note 10, at 590–91 (comparing Chancery's use of dicta to "policymaking devices that agencies routinely and effectively use to influence (if not yet bind) the behavior of actors subject to the agency's regulatory mandate").

57. This Note does not suggest that the "indeterminacy" created by Chancery rulings is suboptimal. Many have argued that the court's case-by-case rulings are superior to SEC

Chancery's opinions have focused on certain factors that may lead to substantial conflicts of interest for an investment bank advising a transacting company. The independence of the advisor may be compromised by, for example, linking a large portion of the advisor's fee to a particular outcome, the advisor's previous relationships with other parties to the transaction, and the advisor's own financial interest in the transaction. The cases that discuss the disclosure of each of these potential conflicts are numerous, but a brief overview will highlight how Delaware has filled the gaps in SEC regulation. Part I.B.1 reviews Chancery's decisions on the disclosure of financial advisor fees. Part I.B.2 examines Chancery's rulings on the disclosure of the financial advisor's relationship with the party on the other side of the proposed transaction. Finally, Part I.B.3 reviews Chancery's decisions on the disclosure of the advisor's financial interest in one of the companies involved in the transaction.

1. *Fees.* — Chancery's decisions on the disclosure of the structure and amount of financial advisor fees have filled gaps in SEC regulations. SEC regulations require only a descriptive summary of the financial advisor's compensation.[58] The SEC staff has often required a quantitative breakdown of the total and contingent amounts of advisor fees, but no legally binding rule requires disclosure of the contingent structure of a fee.[59] Under Delaware law, it is clear that the contingent structure of the fee needs to be disclosed, but whether the amount that is contingent needs to be disclosed as well is unsettled.

In the 2007 case *Louisiana Municipal Police Employees' Retirement System v. Crawford*, Chancery ruled that the contingent nature of an investment bank's compensation must be disclosed when the bank would receive a portion of its fees only upon an "initial favorable recommendation" of the transaction.[60] The same year, the court stated rather perfunctorily that no further details needed to be disclosed when the proxy statement disclosed that the advisor's fee was "customary" and partially contingent.[61] Also in 2007, in a ruling from the bench,[62] Vice Chancellor Lamb

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rules because they allow Chancery to remain adaptable to changing corporate conditions. See, e.g., Leo E. Strine, Jr., The Delaware Way: How We Do Corporate Law and Some of the New Challenges We (and Europe) Face, 30 Del. J. Corp. L. 673, 683 (2005) (noting nature of Delaware corporate lawmaking "allows space for the judiciary to pull back in future cases if a prior decision turns out, in the wake of experience, to have been unwise").

58. See supra Part I.A (describing SEC rules on financial advisor conflicts).

59. See supra notes 47–53 and accompanying text (describing SEC regulation and staff review of advisor fees).

60. 918 A.2d 1172, 1190–91 (Del. Ch. 2007) (noting Chancery "has recognized that the contingent nature of an investment banker's fee can be material and have actual significance to a shareholder relying on the banker's stated opinion").

61. Globis Partners, L.P. v. Plumtree Software, Inc., No. 1577-VCP, 2007 WL 4292024, at *13 (Del. Ch. Nov. 30, 2007). Lloyd L. Drury surmises that Chancery may have applied less scrutiny to potential conflicts in *Globis Partners* because it was not a private equity transaction. Drury, supra note 21, at 61–62, 71 ("When the private equity industry was booming, Delaware was alert and putting shareholders on notice of potential conflicts.

held that, where only eight million dollars of the thirty-three-million-dollar fee was conditional on the completion of the transaction, it was sufficient to disclose that part of the fee was contingent without disclosing the contingent amount, but suggested there might be a "good claim" for quantified disclosure if a larger portion of the fee was conditional.[63]

In *In re Atheros Communications*, Chancery identified such a "good claim"—the court ruled that it was insufficient to disclose that a "substantial portion" of the advisor's fee was contingent on the merger where the actual conditional amount was ninety-eight percent of the fee.[64] Chancery reasoned that a bright line rule for when the contingent amount needs to be disclosed would be "difficult, if perhaps impossible," but that "[r]egardless of where that 'line' may fall, it is clear that an approximately 50:1 contingency ratio requires disclosure."[65] The court suggested that the adequacy of the fee disclosure depends, in part, on the size of the merger.[66]

However, Chancery has suggested the amount of a fee that is conditional on a particular outcome might be material even in the case of a more balanced fee structure. In a bench ruling approving a settlement in *Continuum Capital v. Nolan*, Vice Chancellor Laster noted that while Chancery has been "dismissive" of these types of disclosure claims in the past and every case is different, the use of the term "customary fee" in disclosure does not provide "meaningful insight to stockholders as to the banker's incentives," and, more generally, "the details of the banker's fee are quite important."[67] The case led some to suggest that Chancery was taking a more aggressive tack toward disclosure of the conditional amount of an advisor's fee.[68] Given that Chancery has not come to a con-

When private equity disappeared, so did the scrutiny of alleged disclosure violations."); see also Cnty. of York Emps. Ret. Plan v. Merrill Lynch & Co., No. 4066-VCN, 2008 WL 4824053, at *11 (Del. Ch. Oct. 28, 2008) (ruling it sufficient to disclose fees were partially contingent on consummation of strategic transaction).

62. Vice Chancellor Lamb actually stated that he preferred to make opinions that could be cited and relied upon, but chose to make an oral ruling because of other obligations and market conditions surrounding the transaction. He specifically stated that he "wouldn't consider [it] an opinion," but only a ruling. Transcript of Oral Argument on Plaintiffs' Motion for Preliminary Injunction and Rulings of the Court at 86–87, In re BEA Sys., Inc. S'holder Litig., No. 3298-VCL (Del. Ch. Mar. 26, 2008).

63. Id. at 96.

64. In re Atheros Commc'ns, Inc. S'holder Litig., No. 6124-VCN, 2011 WL 864928, at *8 (Del. Ch. Mar. 4, 2011) (noting "percentage of the fee that is contingent exceeds both common practice and common understanding of what constitutes 'substantial'").

65. Id. at *9.

66. Id. at *9 n.68 (citing Rohrbacher & Zeberkiewicz, Fair Summary, supra note 25, at 899–900) (approvingly citing Rohrbacher and Zeberkiewicz for proposition that more than customary disclosure may be required in multibillion dollar mergers).

67. Transcript of Oral Argument at 97, Continuum Capital v. Nolan, No. 5687-VCL (Del. Ch. Feb. 3, 2011).

68. See, e.g., Blake Rohrbacher & John Mark Zeberkiewicz, Fair Summary II: An Update on Delaware's Disclosure Regime Regarding Fairness Opinions, 66 Bus. Law. 943,

sensus on what contingent fee percentage is "substantial" enough to require disclosure, it is likely difficult for dealmakers to determine what information they need to disclose.

2. *Previous Relationships with the Other Party in a Transaction.* — Shareholders evaluating a financial advisor's recommendation may be interested not only in the fee arrangement, but also in any relationship the advisor has with the company on the other side of the transaction. Chancery has required that filers disclose more than just the "material relationships" that have "existed during the past two years" between the outside advisor and the subject company, which is all that the SEC regulations require.[69] Additionally, Chancery has increasingly scrutinized potential conflicts of interest for employees of the advisor who previously have worked for the other side of a deal, an area of disclosure on which SEC rules and rule interpretations are silent.

Chancery has, in some instances, required more detailed disclosure of the advisor's work for the opposing side of a transaction. In *In re Art Technology Group*, Vice Chancellor Laster enjoined a merger until the parties updated a proxy statement to include further information about the seller's advisor's (unrelated) work for the buyer, including the aggregate compensation paid by the buyer to the advisor for the past four years and a description of the services that the advisor provided the buyer.[70] Laster focused on the potential conflict in the incentives of the seller's advisor because it had received more aggregate fees from the buyer than from the seller during the four-year lead up to the merger.[71] The court's order exceeds SEC requirements by demanding that the disclosure cover a longer period of time and include greater detail about the advisor's services.[72] However, the guidance provided by *Art Technology* may be limited, as the court may have been concerned that the specific facts of

956 (2011) ("[I]t appears that the Delaware courts are likely to require more disclosure of the fees to be paid to a board's financial advisor and of how much of those fees are contingent.").

69. See supra notes 34–35 and accompanying text (describing SEC's disclosure requirement for "material relationships" between outside advisor and subject company and affiliates).

70. In re Art Tech. Grp., Inc. S'holders Litig., No. 5955-VCL, 2010 WL 5184244 (Del. Ch. Dec. 21, 2010).

71. Telephone Conference on Supplemental Disclosure Language and Rulings of the Court at 12–13, *In re Art Tech. Grp.*, 2010 WL 5184244.

72. See supra notes 34–35 and accompanying text (describing SEC's disclosure requirement for "material relationships" during previous two years between outside advisor and subject company and affiliates); see also Ling Kong & Jeffrey Rothschild, Financial Advisor Conflicts Update, McDermott Will & Emery (Mar. 2, 2012), http://www.mwe.com/Financial-Advisor-Conflicts-Update-03-02-2012/?PublicationTypes=d9093adb-e95d-4f19-819a-f0bb5170ab6d (on file with the *Columbia Law Review*) (suggesting ruling exceeded requirements under Regulation M-A).

the transaction skewed the advisor's incentives.[73] Some facts and circumstances clearly warrant disclosure in Delaware. When approving attorney's fees in a recent settlement, Vice Chancellor Glasscock noted that supplemental disclosure stating that one of the buyer's financial advisors had access to the seller's nonpublic financial information "mere months before the announcement" of the merger was material.[74]

Perhaps surprisingly, given its disclosure requirements for institutional relationships, Chancery has not yet chosen to require disclosure of potential conflicts at the employee level. However, certain decisions suggest there is a strong argument for heightened disclosure when individuals have worked on the other side of a deal. Dicta in these opinions have gone further than SEC rules and rule interpretations in pushing for disclosure at the employee level,[75] but the opinions provide minimal guidance on when such an obligation will be triggered.

In *David P. Simonetti Rollover IRA v. Margolis*, an investment bank represented the seller in a transaction one year prior to representing the acquirer.[76] Chancery ruled that the proxy statement need only disclose that the same bank had represented both parties to the merger within a short period—the statement did not need to also disclose that virtually the same team of bankers had represented both sides.[77] However, the court expressed some concern about potential conflicts of interest for the acquirer's banking team, noting its "reservation that [the team] may have acquired some insight into [the seller's] institutional temperament and mood through its interactions with [the seller's] management."[78]

Similarly, Chancery ruled in *In re Zenith National Insurance Corp.* that a proxy statement need not disclose that one of the seller's senior bankers, along with much of his deal team, had worked on a recent engagement for the buyer, because the statement disclosed the key engagements between the bank and the buyer and the total compensation the buyer paid the bank.[79] However, Vice Chancellor Laster decided against enjoinment of the merger on the totality of the circum-

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73. See Telephone Conference on Supplemental Disclosure Language and Rulings of the Court, supra note 71, at 14 (noting ruling on buy-side disclosure in this case was novel and "driven by facts and circumstances").

74. In re PAETEC Holding Corp. S'holders Litig., No. 6761-VCG, 2013 WL 1110811, at *7 (Del. Ch. Mar. 19, 2013).

75. See supra notes 34–35 and accompanying text (describing broad "material relationships" requirement). The general SEC interpretations have not discussed financial advisor conflicts at the employee level.

76. No. 3694-VCN, 2008 WL 5048692, at *6–*7 (Del. Ch. June 27, 2008).

77. Id. at *7.

78. Id. However, the court reasoned that this was a "speculative inference . . . not substantiated in the record" which did not "support a holding of materiality." Id.

79. Transcript of Oral Argument on Plaintiff's Motion for a Preliminary Injunction and Rulings of the Court at 124, In re Zenith Nat'l Ins. Corp., No. 5296-VCL (Del. Ch. Apr. 22, 2010) (distinguishing between material disclosure and merely helpful disclosure).

stances, and refused to draw a bright line rule, noting that the claim was "very close" and that "nobody should cite this transcript as saying 'Court of Chancery blesses same banker working for target side, having six months ago worked for bidder side.'"[80] In oral argument, Laster suggested the fact that the bankers had worked on both sides of a deal within a short time period could be considered material information to voting shareholders.[81] The importance of the specific facts of the case to the decision is clear; Laster even notes that he may have easily ruled the other way if the bank were more involved in the deal.[82]

Dicta in these opinions may suggest the direction in which the court is headed on the issue of employee conflicts, but, given that the decisions in cases like *Simonetti* and *Zenith* are dependent on the type of transaction and extent of advisor involvement, dealmakers will have to determine when their deals warrant disclosure of individual conflicts.[83] While many will likely err on the side of caution and overdisclose, disclosing all potential advisor conflicts at the individual level could lead to overly prolix disclosure statements that would increase transaction costs.[84]

3. *The Advisor's Financial Interest in the Deal.* — While SEC rules and rule interpretations are silent on the issue,[85] Chancery has noted that "[a] financial advisor's own proprietary financial interest in a proposed transaction must be carefully considered in assessing how much credence to give its analysis."[86] Both the advisor and its employees can potentially have a financial interest in the parties involved in a transaction.

In *David P. Simonetti,* Chancery ruled that it was insufficient to disclose that the seller's advisor held some debt obligations of the seller and would receive "cancellation" and "make-whole" payments upon con-

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80. Id. at 122–24 (noting factors leading to his decision, including transaction was arm's-length, advisor was relatively uninvolved, and no one deposed key banker).

81. Id. at 67–68 (suggesting disclosure could include saying "'certain of our people have worked on the teams for,' you know, 'prior engagements'").

82. Id. at 123–24 ("And had any of these factors been different, particularly the role of Merrill in the deal . . . then you would probably be getting an opinion from me Monday or Tuesday enjoining the stockholder meeting.").

83. In an order approving attorney's fees, Vice Chancellor Glasscock recently suggested that the most important supplemental disclosure plaintiffs were able to obtain was that the same *individual* bankers who had access to the seller's financial information later advised the buyer in its acquisition of the seller. In re PAETEC Holding Corp. S'holders Litig., No. 6761-VCG, 2013 WL 1110811, at *7–*8 (Del. Ch. Mar. 19, 2013).

84. Transcript of Oral Argument on Plaintiff's Motion for a Preliminary Injunction and Rulings of the Court, supra note 79, at 70 (noting, from perspective of defense counsel, slippery slope of looking in detail at makeup of deal teams and potential negative effects for "people operating the economy").

85. See supra Part I.A (describing SEC rules and SEC staff's interpretative guidelines).

86. David P. Simonetti Rollover IRA v. Margolis, No. 3694-VCN, 2008 WL 5048692, at *8 (Del. Ch. June 27, 2008).

summation of a merger.[87] The court ordered the seller's board to disclose a range of values for these holdings, even if their quantification was inherently uncertain.[88] In a footnote, however, the court allowed advisors some breathing room, noting that such holdings would only be material if they were "of sufficient magnitude."[89]

In *In re El Paso Corp.*, Chancery noted, in dicta, that both the seller's bank and its lead banker had conflicts of interest.[90] The seller's bank, Goldman Sachs, owned nineteen percent of the buyer's stock, a monetary interest far outweighing its potential merger fees.[91] Chancellor Strine considered the conflict "addressed, albeit in incomplete and inadequate ways," in the proxy statement, but spent much of the opinion criticizing the effect of Goldman's financial interest on the deal process.[92] While the opinion did not seriously fault the disclosure of the bank's conflict of interest, the Chancellor's heightened scrutiny of banks' proprietary interests in a transaction may signal increased disclosure obligations in the future.[93]

On the same day *El Paso* was decided, Vice Chancellor Parsons ruled in *In re Micromet* that a target board's recommendation statement sufficiently disclosed advisor Goldman Sachs's conflict by stating that the bank "may at any time make or hold long or short positions and investments . . . in the equity, debt and other securities of both" companies

87. Id.

88. Id at *9. ("[A]lthough the record indicates that quantifying the value of the warrants will not be an easy undertaking, the Court is satisfied that their value may be quantified.").

89. Id. at *8 n.29.

90. In re El Paso Corp. S'holder Litig., 41 A.3d 432, 448 (Del. Ch. 2012).

91. Id. at 434, 443 (noting Goldman's merger fee was twenty million dollars and Goldman's interest in buyer was worth four billion dollars).

92. Id. at 448 ("Goldman's largest conflict was surfaced fully and addressed, albeit in incomplete and inadequate ways . . . ."). Strine took issue with the level of disclosure, but questioned whether "plaintiffs could ultimately prove Goldman liable for any shortfall." Id. Instead, most of Strine's problems with the advisor's conflict of interest had to do with its effects on the deal process. Id.; see also El Paso Corp., Proxy Statement Pursuant to Section 14(a) of the Securities Exchange Act of 1934 (Schedule 14A), at 27 (Jan. 31, 2012) [hereinafter El Paso Corp., Proxy Statement] ("In addition to . . . [being] a financial advisor to El Paso, Goldman Sachs is also a stockholder of Kinder Morgan and, prior to consummation of the proposed transactions . . . own[s] approximately 19 percent of the shares of Kinder Morgan Class P common stock . . . making it the second largest beneficial holder.").

93. See Eduardo Gallardo, Delaware Court Considers Conflict of Interest in M&A, Harvard Law Sch. Forum on Corporate Governance & Fin. Regulation (Mar. 15, 2012, 8:23 AM), https://blogs.law.harvard.edu/corpgov/2012/03/15/delaware-court-considers-conflicts-of-interest-in-ma/ (on file with the *Columbia Law Review*) ("Chancellor Strine's opinion highlights the continuing heightened level of skepticism that the Court will display towards the actions of fiduciaries and advisors that may appear to be tainted by potential conflicts of interest.").

involved in the transaction.[94] Even though it was representing the seller, Goldman held $336 million in the stock of the buyer, mostly on behalf of its clients.[95] However, the holdings amounted to only "approximately 0.16% of its overall investment holdings and 3.8% of its healthcare sector investments," and Goldman actually had greater holdings in competing bidders.[96] Parsons reasoned that the statement gave sufficient notice to shareholders such that they could choose to look up Goldman's position in either company in Goldman's publicly filed SEC documents.[97]

The approach to the disclosure of Goldman's conflict in *Micromet* is at odds with the attention Chancellor Strine directed to Goldman's conflict in *El Paso*, which was considered "incomplete" even though it provided significant detail about Goldman's interest in the transaction.[98] The size and nature of the holding may be instructive; it is not clear that Strine would have considered the boilerplate *Micromet* disclosure of potential "long or short positions and investments" to be sufficient if Goldman had owned a full nineteen percent of the buyer's stock, like it did in *El Paso*.[99]

In *El Paso*, Chancellor Strine reserved much of his criticism for the Goldman lead banker's personal conflict of interest. The employee's "personal ownership of approximately $340,000" in the buyer's stock was not disclosed, an omission that Strine said was "a very troubling failure," although he decided not to enjoin the merger on the equities.[100] Chancellor Strine's opinion is a good example of Chancery providing clear guidance to future dealmakers because it signals heightened scrutiny of such individual conflicts. The implication may be that individual bankers will have to disclose their own financial interest in a deal if such interest could be material.[101] However, the guidance runs into the same "slippery slope" issue as the opinions on the disclosure of previous

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94. In re Micromet, Inc. S'holders Litig., No. 7197-VCP, 2012 WL 681785, at *11–*12 (Del. Ch. Feb. 29, 2012) (internal quotation marks omitted).

95. Id. at *11.

96. Id.

97. Id. at *12 ("Given this notice, any investor who desired to know the size of Goldman's position in Micromet or Amgen as of the last reporting period could find this information in Goldman's publicly-filed Form 13F.").

98. See supra note 92 and accompanying text (describing Chancellor Strine's characterization of Goldman's disclosure in *El Paso*); see also El Paso Corp., Proxy Statement, supra note 92 (providing language of advisor conflict disclosure in 14A).

99. See supra notes 90–93 and accompanying text (describing Strine's treatment of Goldman's financial interest in *El Paso*).

100. In re El Paso Corp. S'holder Litig., 41 A.3d 432, 442 (Del. Ch. 2012).

101. Matthew Kuhn & Jonathan L.H. Nygren, Addressing Financial Advisor Conflicts in the Wake of *Del Monte* and *El Paso*, Faegre Baker Daniels (July 16, 2012), http://www.faegrebd.com/18685 (on file with the *Columbia Law Review*) ("El Paso introduces the added wrinkle of boards potentially desiring information on individual members of the banking team in addition to information about potential conflicts at a firm level.").

working relationships because, without a clear ex ante requirement, advisors may incur costs to identify personal conflicts before deciding what particular conflicts need to be disclosed.[102]

Again, proper disclosure rests on case-specific facts; the materiality of the financial advisor's interest depends both on its nature and its size, and on the language of the disclosure. Additionally, it is unclear whether materiality is determined through the absolute or the relative value of the financial interest. In *Micromet*, Vice Chancellor Parsons determined that Goldman Sachs's financial interest in the deal was immaterial because it made up a relatively small part of Goldman's holdings,[103] but in *In re Art Technology*, Vice Chancellor Laster required disclosure of fees the buyer paid in the previous four years to the seller's advisor, Morgan Stanley, despite the fees being relatively immaterial to Morgan Stanley's business.[104] Chancery appears to apply different standards of materiality to different kinds of conflicts. With no controlling cases to determine what would be an interest of "sufficient magnitude," dealmakers may risk injunction if they fail to err on the side of disclosing all substantial financial interests in the deal.

II. TWO DIFFERENT KINDS OF "RULEMAKING"

Chancery has created a fiduciary duty-based disclosure regime through its opinions. Given the SEC's congressionally mandated role in promulgating disclosure rules, it is important to examine the implications of Chancery's increasing power to shape disclosure obligations in change-of-control transactions. Part I demonstrated that the SEC and Chancery have created substantively different disclosure rules, with Chancery filling many of the gaps necessarily left open in broad SEC regulations. These dual rulemaking regimes have resulted in unsettled disclosure obligations.[105] Part II of this Note deals with the implications of two very different kinds of disclosure "rulemaking."

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102. See Gina Chon & Anupreeta Das, Goldman Reviewing Policies on Its Deal Makers' Conflicts, Wall St. J. (Mar. 16, 2012), http://online.wsj.com/article/SB10001424052702304459804577285361058353548.html (on file with the *Columbia Law Review*) (indicating banks are beginning to disclose all potential conflicts at employee level).

103. See supra notes 94–97 and accompanying text (discussing *In re Micromet*).

104. Transcript of Oral Argument on Plaintiff's Motion for a Preliminary Injunction and Rulings of the Court at 61, In re Art Tech. Grp., Inc. S'holders Litig., No. 5955-VCL, 2010 WL 5184244 (Del. Ch. Dec. 20, 2010) (noting fees paid by acquirer to target bank were "something like two-hundredths of one percent of their revenue throughout this period"). Laster responded that the previous fees were material because banks may weigh relative fees against each other, even if they are a small part of overall revenue. Telephone Conference on Supplemental Disclosure Language and Rulings of the Court, supra note 71, at 11.

105. See supra Part I (describing SEC disclosure rules and Chancery decisions on disclosure of potential conflicts of financial advisor).

Part II.A describes the SEC's broad authority to regulate disclosure for the benefit of investors. Part II.B compares the rulemaking requirements that govern new disclosure rules promulgated by the SEC and the procedural protections—such as they exist—in Chancery "rulemaking."[106] Part II.C considers the costs of two lawmaking bodies independently creating parallel disclosure regimes. It suggests the status quo may lead to increased uncertainty for dealmakers and results in a missed opportunity for valuable collaboration between the SEC and Chancery.

A. *The SEC's Disclosure Mandate Is Rooted in the 1934 Exchange Act*

A broad disclosure mandate accompanied the SEC's creation, suggesting that Congress favored a federal disclosure regime. From the time of its formation in the Exchange Act, the SEC has undertaken the primary responsibilities of ensuring "fair and honest" securities markets and providing the investing public with adequate disclosure.[107] In passing the Exchange Act, Congress believed that increased disclosure would help uphold the integrity of financial markets after the stock market crash of 1929.[108] Congress considered state disclosure regimes in place at the time to be ineffective and gave the SEC broad powers to establish uniform federal disclosure rules.[109]

The SEC's disclosure requirements explicitly extend to shareholder voting on corporate action. Section 14(a) of the Exchange Act states that "[i]t shall be unlawful for any person . . . in contravention of such rules and regulations as the Commission may prescribe . . . to solicit or to permit the use of his name to solicit any proxy or consent or author-

106. See supra notes 2–3 and accompanying text (discussing how Chancery decisions effectively act as rules for corporate actors).

107. Coffee & Sale, supra note 36, at 55; see also 1 Louis Loss et al., Fundamentals of Securities Regulation 10 (6th ed. 2011) (observing federal securities law is about "disclosure, again disclosure, and still more disclosure").

108. See, e.g., Steven M. Davidoff & Claire A. Hill, Limits of Disclosure, 36 Seattle U. L. Rev. 599, 605 (2013) (noting legislative history of Exchange Act repeatedly refers to disclosure as valuable method of improving integrity of markets); cf. James M. Landis, The Legislative History of the Securities Act of 1933, 28 Geo. Wash. L. Rev. 29, 30 (1959) (noting Exchange Act responded to demand from public for "institution of procedures of governmental control that would . . . control not only the manner in which securities could be issued but the very right of any enterprise to tap the capital market").

109. See, e.g., Mark J. Roe, Delaware's Competition, 117 Harv. L. Rev. 588, 611 (2003) [hereinafter Roe, Delaware's Competition] ("Delaware and other states were seen, when the securities laws were passed, as not having induced information to flow adequately from the corporation to its shareholders."); see also A.A. Sommer, Jr., Comm'r, Sec. & Exch. Comm'n, Current Problems of Disclosure, Address Before the National Association of Securities Dealers, Inc. 6–7 (Nov. 12, 1974), available at http://www.sec.gov/news/speech/1974/111274sommer.pdf (on file with the *Columbia Law Review*) (arguing, in face of contemporary disclosure landscape, "only appropriate answer to such a problem was federal intervention and the establishment of uniform standards, accompanied by a power sufficient to police and enforce them").

ization."[110] According to the legislative history, this section of the Act was intended to prevent the "recurrence of abuses" which had "frustrated the free exercise of the voting rights of stockholders."[111] The purpose was to prevent management from obtaining shareholder authorization for corporate action by "means of deceptive or inadequate disclosure in proxy solicitation."[112] The SEC's disclosure mandate is not limited to shareholder voting; when change of control became increasingly possible via shareholder selling in the context of a tender offer, Congress responded with an Act providing for SEC regulations that protect shareholders by increasing disclosure obligations in that context.[113] Indeed, courts have long recognized the SEC's role in requiring companies to provide information to shareholders to permit informed voting and tendering.[114]

Given the SEC's mandate to protect investors through disclosure, it is not surprising that federal rulemaking often takes the form of new disclosure obligations, displacing prior state law.[115] Under the Supremacy Clause,[116] SEC disclosure rules may preempt state disclosure law. Examples of SEC rules preempting their state counterparts include those regulating disclosure of executive compensation,[117] going-private transactions, and certain tender offer transactions.[118]

However, the creation of the SEC did not entirely displace state disclosure law. Section 28(a) of the Exchange Act provides that "the

110. Securities Exchange Act of 1934 § 14(a), 15 U.S.C. § 78n(a)(1) (2012).

111. H.R. Rep. No. 73-1383, at 14 (1934).

112. J.I. Case Co. v. Borak, 377 U.S. 426, 431 (1964), abrogated on other grounds by Cort v. Ash, 422 U.S. 66, 78 (1975), as recognized in Alexander v. Sandoval, 532 U.S. 275, 287 (2001).

113. See Williams Act of 1968, Pub. L. No. 90-439, 82 Stat. 454 (codified as amended at 15 U.S.C. §§ 78m(d)–(e), 78n(d)–(f) (2012)); Robert B. Thompson, Preemption and Federalism in Corporate Governance: Protecting Shareholder Rights to Vote, Sell, and Sue, Law & Contemp. Probs., Summer 1999, at 215, 220 (noting Congress extended shareholder protection when "shareholders were being asked to make a decision without sufficient information," although this time not "a decision about voting," but rather a decision "whether to sell their shares in response to a bidder's tender offer").

114. See supra note 21 (discussing cases recognizing such role for SEC).

115. See Thompson, Delaware's Disclosure, supra note 17, at 177 ("The dominant pattern is that the federal government has regularly chosen to channel its corporate governance law making through disclosure without changing the basic substantive relationship among the core parties as determined by state law.").

116. U.S. Const. art. VI, cl. 2.

117. See Thompson, Delaware's Disclosure, supra note 17, at 180 ("[T]he still new SEC disclosure rules regarding executive compensation have been the most important legal change relating to that topic, dwarfing the impact of state law on that subject." (citing 17 C.F.R. § 229.402 (2008))).

118. See Roe, Delaware's Competition, supra note 109, at 616–17, 619 (noting Rule 13e-3 was meant to overturn Delaware common law on going-private transactions and "all holders rule" (Rules 13e-4 and 14d-10) was meant to overturn Delaware common law on self-tenders).

rights and remedies provided by this chapter shall be in addition to any and all other rights and remedies that may exist at law or in equity,"[119] preserving rights and remedies under state statutory and common law. Thus, section 28(a) leaves states room to overlay state-specific disclosure laws on SEC disclosure rules through both state legislatures and state courts.[120]

Preemption, therefore, is limited to those state laws that conflict with, or stand as obstacles to, the purpose of federal disclosure rules.[121] Preemption of disclosure rules is not often litigated because most challenged state law in the area of disclosure does not conflict with—but instead supplements—federal securities regulation.[122] Chancery's case law on the disclosure of financial advisor conflicts falls into the category of "supplemental" rules, but new SEC rulemaking could preempt Delaware law if the latter stands as an obstacle to the federal regulation.[123]

B. *Comparing the Procedural Protections of SEC and Chancery "Rulemaking"*

The SEC and Chancery both create disclosure rules for dealmakers, but their rulemaking procedures are very different. The procedural requirements of SEC rulemaking and the Administrative Procedure Act[124] (APA) mandate a rigorous notice-and-comment period and set out certain standards of judicial review. The combination of Chancery's use of dicta to provide forward-looking guidance and the court's engagement with the dealmaking community has allowed it to capture some of the procedural benefits of a formalized rulemaking process. Nevertheless, the lack of mandated notice-and-comment protections and a different style of judicial review distinguish Chancery's disclosure rulemaking. Part II.B.1 describes the procedural and judicial protections that govern SEC rulemaking. Part II.B.2 distinguishes both Chancery's approximation of notice-and-comment "rulemaking" and the judicial review of Chancery decisions by the Delaware Supreme Court.

119. Securities Exchange Act of 1934 § 28(a), 15 U.S.C. § 78bb(a)(2) (2012).

120. See Francis J. Facciolo & Richard L. Stone, Avoiding the Inevitable: The Continuing Viability of State Law Claims in the Face of Primary Jurisdiction and Preemption Challenges Under the Securities Exchange Act of 1934, 1995 Colum. Bus. L. Rev. 525, 540 (noting "presence of section 28(a)" means "there has been only a limited consideration" of field preemption in cases involving potential preemption of state law by Exchange Act).

121. See id. at 538 ("Only directly conflicting state schemes or state statutes which frustrate a purpose clearly articulated in a federal securities law are preempted.").

122. Id. at 538–39.

123. See infra Part III.A (describing potential for SEC preemption in this space as potential method for reconciling SEC disclosure mandate and Chancery disclosure rulings).

124. The APA governs how federal agencies propose and establish regulations. It also gives standards for the judicial review of agency decisions by U.S. federal courts. 5 U.S.C. §§ 500–596 (2012).

1. *SEC Rulemaking Procedure and Judicial Review.* — Under SEC regulations, which generally incorporate the informal rulemaking procedures of the APA,[125] there are certain requirements for making and changing (as opposed to interpreting) rules: The SEC must give notice of the pending rulemaking proceeding, must identify the statutory authority under which the rule will be promulgated, and must describe the proposed rule.[126] The SEC is required to publish the proposed rule in the Federal Register and seek comments from interested parties, which are made part of the public record.[127] For the adoption of rules "materially affecting an industry or a segment of the public," the SEC must make "every feasible effort" to receive the views of affected persons in advance of adoption.[128] The comments may be submitted online and all written comments, including paper comments, are viewable on the SEC's website.[129] The SEC must analyze submitted comments before crafting the final rule.[130] The D.C. Circuit has noted that if the commentary presents reasonable alternatives, "the agency must either consider those alternatives or give some reason . . . for declining to do so."[131] The comment process often leads to the SEC "substantially adjusting, amending, or even scrapping its original proposals."[132]

The statutory notice-and-comment procedure is reinforced by judicial review, which may be deferential to agency actions but often takes a closer look at SEC rulemaking. Under the APA, a reviewing court will invalidate an agency action that is "in excess of statutory jurisdiction, authority, or limitations, or short of statutory right."[133] Under *Chevron*, a court reviewing agency actions uses a deferential standard of review: If Congress spoke directly to the precise question at issue, then that is the end of the matter, but if the statute is silent or ambiguous with respect to

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125. See § 553 (listing APA rulemaking procedures).

126. 17 C.F.R. § 201.192(b) (2012).

127. § 202.6(b).

128. § 202.6(a).

129. See How to Submit Comments, Sec. & Exch. Comm'n, http://www.sec.gov/rules/submitcomments.htm (on file with the *Columbia Law Review*) (last modified May 9, 2013) (describing submittal methods and noting all comments will be publicly viewable).

130. § 202.6(c); see also 5 Thomas Lee Hazen, Treatise on the Law of Securities Regulation § 16.36[2], at 147 (5th ed. 2005) ("After the Commission has reviewed the comments, the rule may be adopted in its original or in a revised form or a revised draft may be published and comments on the revised draft may be filed with the Commission."). The APA also requires agencies to consider the "relevant matter presented" by the comments. 5 U.S.C. § 553(c).

131. Laclede Gas Co. v. FERC, 873 F.2d 1494, 1498 (D.C. Cir. 1989) (emphasis omitted); see also Chamber of Commerce of U.S. v. SEC, 412 F.3d 133, 145 (D.C. Cir. 2005) (holding proposed "disclosure alternative was neither frivolous nor out of bounds and the Commission therefore had an obligation to consider it").

132. Prentice, supra note 12, at 801–02.

133. 5 U.S.C. § 706(2)(C).

the specific question, the court determines whether the SEC's interpretation is "based on a permissible construction of the statute."[134]

However, a more rigorous scrutiny of agency actions may often apply to SEC rulemaking. Under the APA, in addition to actions that exceed statutory jurisdiction, courts will set aside any agency action that is "arbitrary, capricious, an abuse of discretion, or otherwise not in accordance with law."[135] Courts have developed a "hard look" standard of review based on the arbitrary and capricious language of the APA.[136] The hard look standard of review is applied to SEC rulemaking more frequently than *Chevron* deference.[137] Although the scope of review under the hard look standard is narrow and judges are not supposed to substitute their judgment for that of the agency, courts will make sure that the SEC has "'examine[d] the relevant data and articulate[d] a satisfactory explanation for its action including a rational connection between the facts found and the choice made.'"[138] Because it is a process-based review, courts conducting hard look review require that agencies offer detailed explanations for their conclusions, respond to reasonable counterarguments, justify departures from past practices, and carefully consider proposed alternatives.[139] However, many scholars note that judges may inject their own policy preferences into hard look review and engage in a substantive review of agency actions.[140]

In recent D.C. Circuit cases, the court has noted that the SEC also has a unique statutory obligation to consider a proposed rule's effect on

134. Chevron U.S.A. Inc. v. Natural Res. Def. Council, Inc., 467 U.S. 837, 842–43 (1984).

135. § 706(2)(A).

136. See, e.g., Motor Vehicle Mfrs. Ass'n v. State Farm Mut. Auto. Ins. Co., 463 U.S. 29, 43 (1983) (elaborating on more stringent review of agency actions).

137. Jill E. Fisch, The Long Road Back: *Business Roundtable* and the Future of SEC Rulemaking, 36 Seattle U. L. Rev. 695, 710–11 (2013) [hereinafter Fisch, Long Road] (describing frequency of "hard look review" of agency actions as compared to deferential review under *Chevron*).

138. Chamber of Commerce of U.S. v. SEC, 412 F.3d 133, 140 (D.C. Cir. 2005) (alternation by *Chamber of Commerce*) (quoting *Motor Vehicle Mfrs.*, 463 U.S. at 43); see also Thomas J. Miles & Cass R. Sunstein, The Real World of Arbitrariness Review, 75 U. Chi. L. Rev. 761, 768 (2008) ("A key goal of the arbitrary and capricious standard is to ensure that judges invalidate agency actions when those actions reflect serious analytic errors or palpable political pressures, and to prevent these errors and pressures from being translated into grounds for law.").

139. See Miles & Sunstein, supra note 138, at 761 ("The doctrine found its origins in judicial decisions requiring administrative agencies to demonstrate that they had taken a 'hard look' at the underlying questions of policy and fact.").

140. See Fisch, Long Road, supra note 137, at 711 (showing empirically "hard look review appears to have morphed from process-based review into substantive review, with the court overturning agency decisions on the basis of its own policy preferences" (footnote omitted)). See generally Miles & Sunstein, supra note 138, at 774–89 (empirically showing ideological perspectives of judges have significant effect on whether courts strike down agency actions under hard look review).

"efficiency, competition, and capital formation."[141] A rule will be determined to be arbitrary and capricious if the SEC fails to adequately consider the economic consequences of its adoption.[142] To pass muster with a reviewing court, the agency may be required, during its rulemaking process, to adequately discuss the costs and benefits of a rule, quantify the costs of a rule or explain why they could not be quantified, support predictive judgments, and respond to substantial problems raised in comments.[143] When rejecting SEC rules under this standard, the D.C. Circuit has castigated the SEC for the inadequacy of its cost-benefit analysis, and has appeared to substantively review much of the SEC's economic assessment in determining that its rulemaking process was arbitrary and capricious.[144]

2. *Chancery "Rulemaking" Procedure and Judicial Review.* — Chancery is a unique court that has appropriated some of the rulemaking protections of a regulatory agency. Chancery may have captured some of the procedural benefits of an informed notice-and-comment period in its desire to create the best possible corporate law for affected parties.[145] However, there are considerable differences between Chancery's "rulemaking" procedure and the SEC's statutorily mandated rulemaking procedure. Additionally, judicial review of Chancery decisions is uncommon and very different from the process-based review of SEC rulemaking.

Given that Chancery's decisions function as rules for almost the entire set of corporate actors,[146] its opinions serve as "notice" to the dealmaking community. As noted previously, Chancery can use both dicta and holdings to indicate the direction it is moving.[147] However, it is important to note that its ability to use dicta to highlight the direction of

141. Bus. Roundtable v. SEC, 647 F.3d 1144, 1148 (D.C. Cir. 2011) (citing 15 U.S.C. §§ 78c(f), 78w(a)(2), 80a-2(c) (2006)).

142. See *Chamber of Commerce*, 412 F.3d at 143 (noting circumstances in case did not excuse SEC "from its statutory obligation to determine as best it c[ould] the economic implications of the rule it ha[d] proposed").

143. See *Bus. Roundtable*, 647 F.3d at 1148–49 (finding SEC decision to apply rule without adequately doing these things was arbitrary); see also Michael E. Murphy, The SEC and the District of Columbia Circuit: The Emergency of a Distinct Standard of Judicial Review, 7 Va. L. & Bus. Rev. 125, 168–69 (2012) (describing how recent cases have created "gauntlet of obstacles" for "regulations amending the Exchange Act" and subsequently listing such potential obstacles).

144. See Fisch, Long Road, supra note 137, at 699–705 ("[T]he court's statements were less about the SEC's failure to assess costs and benefits than the SEC's erroneous enforcement.").

145. See Savitt, supra note 10, at 592 ("The professional and scholarly network that evaluates Chancery's work permits early consideration and fine-tuning of doctrinal developments.").

146. See supra note 3 and accompanying text (describing how majority of companies incorporate in Delaware and thus Delaware laws act as rules for nearly all corporate actors).

147. See supra notes 83–86 and accompanying text (discussing Chancery's innovative use of dicta).

Delaware law is limited by the facts before it; Chancery has been rebuked by the Delaware Supreme Court in the past for addressing issues beyond those presented to it.[148] Despite those limits, Chancery's dicta in its decisions on the disclosure of financial advisor conflicts provide useful guidance to future actors.[149]

After providing prospective guidance to dealmakers, Chancery can seek out the commentary of the transactional community, which influences the development of its rules in a process that looks like regulatory notice-and-comment rulemaking. The champions of Chancery have often touted its active engagement with deal practitioners and academics as a unique attribute of the court.[150] The specialized nature of Chancery and the corporate expertise of its judges distinguish it from other courts, placing it at the center of a specific area of the law.[151] Members of the court interact regularly with leading transactional actors and scholars,[152] and Chancery decisions are subject to extensive analysis in specialized journals and blogs.[153] Although unusual for judges, the chancellor and vice chancellors spend much time writing and responding to commentary during their tenure, similar to agencies responding to comments on proposed rules.[154] Indeed, Chancery has carefully considered scholarly commentary when developing its "rules" in the past.[155]

148. See, e.g., Gatz Props. v. Auriga Capital Corp., 59 A.3d 1206, 1218–20 (Del. 2012) (rebuking Chancellor Strine for interpreting issue regarding Delaware statute in dicta when issue was not being litigated).

149. See, e.g., supra note 100 and accompanying text (describing how dicta in *El Paso* provides guidance to future dealmakers).

150. Savitt, supra note 10, at 591 (discussing Chancery's unusual engagement with lawyers and academics and its exposure to "commentators who propose, predict, and critique developments in M&A law"); Steele & Verret, supra note 55, at 213 (noting "Delaware judges' direct involvement with constituencies interested in the development of the law at a practical, as well as at a theoretical level").

151. See Savitt, supra note 10, at 591–92 ("Chancery is for these reasons unusual among courts, perhaps unique, in the intensive way in which it interacts with the community that it regulates.").

152. See Lawrence A. Hamermesh, The Policy Foundations of Delaware Corporate Law, 106 Colum. L. Rev. 1749, 1759–60 (2006) (noting Delaware judges often participate in conferences in which they interact "with lawyers . . . other judges, bankers, institutional shareholder representatives, and . . . academics"); Savitt, supra note 10, at 591 ("The members of the Court [of Chancery] make time to participate in conferences dedicated to corporate and transactional law . . . where they hear from, and are heard by, those who study, structure, and litigate transactions.").

153. Savitt, supra note 10, at 591–92; see also, e.g., id. at 592 n.59 (listing publications and blogs often discussing Chancery rulings, doctrines, and related issues in corporate governance and mergers and acquisitions litigation).

154. The current Chancellor is frequently published in law reviews. E.g., Leo E. Strine, Jr., Our Continuing Struggle with the Idea That For-Profit Corporations Seek Profit, 47 Wake Forest L. Rev. 135 (2012). For an example of a chancellor responding to academic commentary, see, e.g., Leo E. Strine, Jr., Response, Toward a True Corporate Republic: A Traditionalist Response to Bebchuk's Solution for Improving Corporate

The "comment" aspect of Chancery's approximation of notice-and-comment rulemaking is still very different than that of the SEC. Unlike with SEC rulemaking, there is no actual requirement for Chancery to consider the commentary of interested parties in its rulings, nor is there a requirement to consider reasonable alternatives suggested.[156] Additionally, Chancery does not have to make every feasible effort to receive commentary as it shapes disclosure obligations.[157]

Importantly, the commentary that Chancery does consider may reflect a different set of interests than those reflected by the commentary considered by the SEC in its rulemaking. Many have argued that, as a result of the state's large financial incentive to maintain its primacy in incorporation, Delaware law is overly responsive to the interests of management.[158] Others have responded that Delaware law carefully considers the interests of both management and shareholders, because laws that come at the expense of the latter would hurt shareholder value and ultimately lead to incorporation elsewhere.[159] However, even if the set of interests that is commonly represented in Delaware courts includes those of current shareholders, there may still be other parties whose interests are underrepresented. Those excluded may include takeover bidders,

America, 119 Harv. L. Rev. 1759 (2006) (responding to Lucian Arye Bebchuk, The Case for Increasing Shareholder Power, 118 Harv. L. Rev. 833 (2005)).

155. See Savitt, supra note 10, at 593–94 (discussing how Chancery has considered scholarly commentary in development of particular judicial standards within Delaware law).

156. Cf. supra notes 125–132 and accompanying text (describing SEC statutory rulemaking requirements).

157. Cf. supra note 127 and accompanying text (noting this requirement in SEC rulemaking context).

158. See, e.g., Cary, supra note 11, at 668–69, 701 (suggesting fees from incorporation incentivize Delaware law to favor management at expense of "modern constituency of the corporation—employees, consumers, and the public, as well as shareholders"); Renee M. Jones, Rethinking Corporate Federalism in the Era of Corporate Reform, 29 J. Corp. L. 625, 636–37 (2004) (noting, though nationally dispersed shareholders lack direct political influence in Delaware, management interests are well represented there, whereas "[s]ophisticated and organized aggregations of shareholders can and do lobby Congress and the SEC to ensure that shareholder interests are considered").

159. See Daniel R. Fischel, The "Race to the Bottom" Revisited: Reflections on Recent Developments in Delaware's Corporation Law, 76 Nw. U. L. Rev. 913, 919–20 (1982) ("If incorporation in Delaware were really harmful to shareholders, shares of firms located there would trade for less, managers would reduce the value of their services, and the firm might be an attractive takeover candidate with the probable result that existing managers would be displaced."); Ralph Winter, Private Goals and Competition Among State Legal Systems, 6 Harv. J.L. & Pub. Pol'y 127, 128 (1982) (noting "corporation in a state that writes its law so as to allow management to siphon off money from other factors of production will find that its earnings go down," leading to higher costs of capital and lower share prices, incentivizing buyers to acquire and reincorporate elsewhere to reap gains).

challenging shareholders, and many affected third parties,[160] such as financial advisors. Many "national" interests may not be represented in Chancery either, including not only those of the general public, but also the concerns of various public interest groups, institutions such as the Federal Reserve and the SEC, and individual policymakers, economists, and academics.[161] Thus, the SEC arguably takes into consideration the commentary of a broader set of interests than that represented in Chancery.[162]

Judicial review of Chancery decisions is different from judicial review of SEC rulemaking. Importantly, Chancery decisions are not commonly subject to review by the Delaware Supreme Court.[163] Chancery hears a large number of cases and relatively few are appealed.[164] Especially in cases stemming from alleged disclosure deficiencies in ongoing transactions, parties may prefer to comply with a court order and close the transaction rather than take the time to appeal Chancery's disclosure rulings.[165] The immediate demands of the transactional market limit judicial review in certain time-sensitive situations.[166] In addition, the overall reversal rate of Chancery decisions is very low.[167] Given this deference by

160. See Lucian Arye Bebchuk, Federalism and the Corporation: The Desirable Limits on State Competition in Corporate Law, 105 Harv. L. Rev. 1435, 1485–94 (1992) (listing takeover bidders and challenging shareholders as interests harmed by laws favoring management and target shareholders, in addition to noncapital-providing constituents such as "workers, communities . . . , consumers, and . . . the environment").

161. See Mark J. Roe, Delaware's Politics, 118 Harv. L. Rev. 2491, 2501–02 (2005) (discussing how national interests such as these do not receive attention in Delaware, which focuses on controlling line between management and investors).

162. See, e.g., Davidoff, Takeover Regulation, supra note 12, at 265–66 ("The SEC takes into account national interests rather than the narrow ones that Delaware acts upon.").

163. See William B. Chandler III & Anthony A. Rickey, Manufacturing Mystery: A Response to Professors Carney and Shepherd's "The Mystery of Delaware Law's Continuing Success," 2009 U. Ill. L. Rev. 95, 104–05 (2009) (discussing Delaware's relatively low rates of appeal and reversal).

164. See Steven M. Davidoff, A Case Study: *Air Products v. Airgas* and the Value of Strategic Judicial Decision-Making, 2012 Colum. Bus. L. Rev. 502, 549 [hereinafter Davidoff, Case Study] (noting most Chancery decisions are not appealed); see also Chandler & Rickey, supra note 163, at 104–05 (discussing low appeal rate); Veasey with Di Guglielmo, supra note 8, at 1408 (noting Chancery's "heavy caseload" and relatively low rate of appeal from Chancery decisions).

165. See In re Del Monte Foods Co. S'holders Litig., 25 A.3d 813, 839 (Del. Ch. 2011) ("Any delay subjects the Merger to market risk. All else equal, a longer delay means greater risk."); see also Veasey with Di Guglielmo, supra note 8, at 1408 (arguing low appeal rate is in part due to "practical reality that [a] business must move on from the answer provided by the Court of Chancery").

166. See Fisch, Peculiar Role, supra note 10, at 1087 (noting "during the 1980s, the rapid transactional demands in the takeover market resulted in the resolution of many cases before they could be reviewed by the [Delaware] supreme court").

167. See Chandler & Rickey, supra note 163, at 104–05 (noting overall reversal rate in 2002 was 0.26%); see also Davidoff, Case Study, supra note 164, at 535 (noting Delaware "[l]ower court decisions frequently diverge and set competing rules, conflicts that the

the Delaware Supreme Court to Chancery, there is unlikely to be stringent and timely review of Chancery disclosure rules.

Judicial review of some disclosure "rules" may be further limited because Chancery's forward-looking dicta is insulated from judicial review. The Delaware Supreme Court will not get a chance to rule on dicta unless a case is appealed, but transactional actors may nevertheless be guided by Delaware judges' increased scrutiny of various potential conflicts of interest.[168] For example, in *El Paso*, Chancellor Strine criticized the disclosure of both the financial advisor's and its individual banker's conflicts, but did not enjoin the merger vote because the bid represented the best offer.[169] The defendants did not appeal on the issue of financial advisor conflicts because their merger escaped injunction, but the Chancellor's forceful dicta remains, at most, a Chancery "rule," and, at least, informal guidance.[170]

Finally, judicial review of Chancery decisions does not reinforce consideration of public commentary or impose any obligation to determine the economic consequences of Chancery-created disclosure rules. When a Chancery decision is appealed, the Delaware Supreme Court is not required to ensure that Chancery has adequately considered comments by anyone apart from the parties before it.[171] Chancery is not burdened with any requirement to consider and quantify the costs and benefits of its disclosure rules, and the Delaware Supreme Court is thus unlikely to strike down a Chancery decision for inadequate consideration of its effect on efficiency, competition, and capital formation.[172] There are no cases in Delaware analogous to those in the D.C. Circuit formalizing what is essentially a substantive review procedure for the economic conse-

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Delaware Supreme Court often avoids resolving"); Stephen Lamb et al., Delaware Double Play, M&A J., June 2009, at 1, 1 (noting reversals of Court of Chancery are rare in merger context).

168. See supra note 101 and accompanying text (discussing increased disclosure of potential financial advisor conflicts at employee level as result of recent Chancery decisions).

169. In re El Paso Corp. S'holder Litig., 41 A.3d 432, 449 (Del. Ch. 2012) ("Unlike a situation when this court will enjoin a transaction whose tainted terms are precluding another available option that promises higher value, no rival bid for El Paso exists.").

170. See supra note 102 and accompanying text (describing how companies are taking precautions to disclose more of their financial advisor conflicts as result of dicta in *El Paso*).

171. Cf. supra notes 133–140 and accompanying text (describing process-based judicial review under APA).

172. Cf. supra notes 141–144 and accompanying text (discussing D.C. Circuit decisions requiring cost-benefit analysis of SEC rules).

quences of rules.[173] As compared to challenged SEC rulemaking, judicial review of Chancery disclosure decisions is likely less stringent.[174]

C. *The Existence of Two Disclosure Regimes Increases Costs and Necessitates Harmonization*

Both the SEC and Chancery have respective institutional advantages and add value to the law regulating disclosure. However, maintaining two wholly independent disclosure rulemakers increases uncertainty for dealmakers and denies the law the benefits of increased collaboration between the SEC and Chancery. The inconsistencies in rules and rulemaking for disclosure in change-of-control transactions suggest that harmonization would be desirable.

Chancery and the SEC each possess valuable characteristics that make them effective disclosure rulemakers. Chancery is well situated to regulate disclosure in change-of-control transactions in a complex and rapidly evolving corporate landscape. Chancery has immense exposure to corporate disputes and shareholder litigation, and has developed a unique expertise in corporate law.[175] Chancery judges are experts in corporate governance, fiduciary duty, and mergers and acquisitions (M&A) law.[176] As noted before, Chancery is highly attuned to developments in the dealmaking community.[177]

As a specialized court of equity with a relatively small docket, Chancery can react quickly to changing business conditions by adjusting disclosure obligations. The court hears many similar cases in rapid succession without a jury to slow down proceedings, increasing its exposure to emerging disclosure trends.[178] Indeed, many Chancery cases involve

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173. See supra note 144 and accompanying text (describing D.C. Circuit as effectively performing substantive review under guise of procedural review of economic analysis).

174. See Fisch, Long Road, supra note 137, at 701–04 (discussing string of cases challenging SEC rules over past eight years in D.C. Circuit, none of which SEC has won).

175. See supra notes 1–3 and accompanying text (discussing Chancery's unusual expertise and exposure).

176. See Savitt, supra note 10, at 585 ("[T]he five Chancery judges are appointed on the basis of their expertise in Delaware corporate law and cannot help but become even more expert by virtue of their deep and continuous exposure to that law and their obligation to interpret and expound it daily and at length."); see also Roe, Delaware's Competition, supra note 109, at 594 ("The judges take pride in keeping up with business trends, having good business sense, knowing their own limits, and reacting quickly as professionals.").

177. See supra notes 150–154 and accompanying text (describing Chancery's integration into dealmaking community).

178. See Fisch, Peculiar Role, supra note 10, at 1086 (noting characteristics facilitating Chancery's unusual ability to respond quickly to developments in business world). Fisch explains that "the court['s] historic receptiveness to requests for expedited proceedings," its "willingness to issue rulings quickly in the context of a fast-paced business transaction," its specialized jurisdiction, its nature as a court of equity that sits without

requests for expedited relief in the context of an ongoing transaction, meaning that the court can respond to disclosure issues as soon as they arise in disputed deals.[179] Because Chancery is relatively flexible and willing to reverse itself, it can also adapt its own jurisprudence as new developments arise.[180]

Chancery is also less likely to create inefficiently burdensome disclosure rules due to political pressure. Unlike the SEC, Chancery is not subject to congressional oversight, and will not be as responsive to pressure from the executive or legislative branch.[181]

The SEC has its own institutional advantages. SEC disclosure rules may be more credibly relied upon than Chancery's decisions given the SEC's disclosure mandate and the possibility of federal preemption of state law.[182] The SEC also has access to greater resources than Chancery, with the ability to devote more personnel, time, and money to studying, receiving commentary on, and improving disclosure policies.[183]

The SEC may draw commentary on its rulemaking process from a broader set of national interest holders than Chancery, including many whose interests are affected by disclosure rules.[184] For example, rules determining the disclosure of financial advisor conflicts will affect the investment banks whose information is being disclosed, even though those banks will not always be directly involved in state disclosure litigation.[185] It may be that the SEC is a better regulator for financial advisor-

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juries, and its relatively small docket size all allow Chancery to respond to "hot" issues in the merger market. Id.

179. See id. ("The procedural context of many chancery court decisions, in which the court is ruling on a request for expedited relief, allows the court to provide tentative guidance about a fast-paced business development while awaiting a full factual record before committing itself.").

180. See id. at 1088 (arguing "flexibility is a function of the atypical nature of Delaware corporate decisional law and causes the chancery court[], in particular, to act something like [an] administrative agenc[y]"); see also supra note 10 and accompanying text (describing Chancery flexibility).

181. See Roe, Delaware's Competition, supra note 109, at 641–43 (describing how SEC positions have changed over time due to policy preferences of executive branch and Congress and political saliency of certain corporate issues); see also Fisch, Peculiar Role, supra note 10, at 1092–95 (identifying advantages of Delaware courts' "independence from political influence").

182. See supra notes 115–118 and accompanying text (describing possibility of federal preemption of state corporate law).

183. See Davidoff, Takeover Regulation, supra note 12, at 266 ("[T]he SEC has the resources of the federal government at its disposal. The SEC can use these to support research, review developments, and continually study issues. It has superior personnel quality and numbers and consequently more capacity for enforcement action and regulation.").

184. See supra notes 158–162 and accompanying text (describing possibility of different sets of interests represented in Chancery and SEC).

185. For evidence that Delaware may have limited influence over financial advisor disclosure, see Vice Chancellor Laster's statement in Transcript of Oral Argument at 44,

related disclosure due to its regular interaction with investment banks.[186] Given increased scrutiny of investment banks recently, a national notice-and-comment period may also allow greater consideration of commentary from groups interested in such rules, including public interest organizations, economists, and national institutions.[187]

While both the SEC and Chancery have their own institutional advantages, the law may benefit from increased harmonization between the two entities. The combination of SEC and Chancery rules has created uncertainty with regard to the required extent of disclosure of financial advisor conflicts. Uncertain disclosure rules are disfavored in corporate law, which aims to reduce transaction costs for dealmakers.[188] Currently, practitioners have to look at two sets of different disclosure rules to determine their obligations in a change-of-control transaction. The SEC has promulgated broad rules based on disclosing "material relationships" and used specific, nonbinding staff review to highlight additional disclosure requirements.[189] In some areas, Chancery has pushed no further than the SEC; for example, neither entity has created a bright line rule for the disclosure of contingent fee amounts, even if SEC staff often require such disclosure.[190] Nevertheless, Chancery has pushed further than the SEC in the disclosure of previous working relationships with the opposing side of a transaction when the facts warrant it,[191] and has highlighted conflicts of interest at the employee level in dicta, suggesting an increase in scrutiny in an area heretofore not addressed by SEC rules and

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Continuum Capital v. Nolan, No. 5687-VCL (Del. Ch. Feb. 3, 2011) ("I get the feeling that a lot of these disclosures are driven by banker's counsel's own willingness to put information in a proxy statement. It's too bad the bankers can't be required to pay the fee.").

186. See, e.g., Turmoil in the U.S. Credit Markets: The Genesis of the Current Economic Crisis: Hearing Before the S. Comm. on Banking, Hous., & Urban Affairs, 110th Cong. 7 (2008) (statement of Arthur Levitt, Jr., Senior Advisor, The Carlyle Group, and former Chairman, Sec. & Exch. Comm'n) (calling SEC "crown jewel of financial regulatory infrastructure"). But there is also the potential that the interests of financial services companies will unduly influence the SEC. See, e.g., Daniel Kaufmann & Veronika Penciakova, Op-Ed., Judge Rakoff Challenge to the S.E.C.: Can Regulatory Capture Be Reversed?, Brookings Inst. (Dec. 2, 2011), http://www.brookings.edu/research/opinions/2011/12/02-rakoff-challenge-kaufmann (on file with the *Columbia Law Review*) (noting SEC's history of regulatory capture).

187. Compare supra note 127 and accompanying text (requiring SEC to receive views of interested parties when adopting rules), with text accompanying note 157 (noting lack of requirement for Chancery to receive commentary), and notes 158–161 and accompanying text (describing how certain national interests are not necessarily represented in Chancery).

188. See Carney & Shepherd, supra note 13, at 5–6 (discussing corporate law's preference for reduced transaction costs and how well-defined rules accomplish goal).

189. See supra Part I.A (discussing SEC financial advisor conflict disclosure rules).

190. See supra Part I.B.1 (discussing Chancery rulings on disclosure of contingent fees).

191. See supra Part I.B.2 (discussing Chancery rulings on financial advisor's previous working relationships with other side of transaction).

interpretive guidelines.[192] As Chancery continues to issue rulings in this area, dealmakers looking to disclose conflicts will have to consider compliance with two different regimes, increasing transaction costs.

Furthermore, maintaining two distinct disclosure rulemakers denies the law the benefit of their collaboration. Both the SEC and Chancery have comparative advantages as rulemakers.[193] Increased collaboration between the two entities may assist in creating efficient and flexible disclosure rules that accommodate a broader set of affected interests.

For example, Chancery's heightened scrutiny of financial advisor conflicts at the individual employee level may reflect concern over the increased potential for bankers to work for both sides of a deal in a short period of time due to consolidation in the financial services industry and the move away from exclusive banker and client relationships.[194] Chancery's specialization in mergers and constant communication with academics and practitioners may assist in crafting rules that do not result in overly burdensome disclosure of individual conflicts of interest.[195] However, subjecting the rules to the SEC's notice-and-comment process may result in valuable input from parties that may receive less consideration in Chancery, such as public interest groups, governmental organizations, and even financial advisors themselves.[196]

III. RECONCILING SEC'S DISCLOSURE MANDATE WITH UNIQUE ATTRIBUTES OF CHANCERY

While Chancery and the SEC each possess characteristics useful for regulating disclosure, the lack of harmonization between the two rulemakers increases uncertainty for actors trying to comply with both disclosure regimes. Any potential solution must reduce these transaction costs for dealmakers and reconcile the SEC's disclosure mandate and Chancery's increased activity in this area of corporate law. Part III.A discusses the more extreme method, which is for the SEC to unilaterally create federal rules that effectively preempt Delaware law. SEC preemption will reduce uncertainty but eliminate the benefits of Chancery's institutional advantages. Part III.B proposes an ultimately superior solu-

192. See supra Part I.B.3 (discussing Chancery rulings on financial advisor's financial interest in transaction).

193. See supra notes 175–187 and accompanying text (comparing institutional rulemaking advantages of each entity).

194. David Fox & Daniel E. Wolf, Kirkland M&A Update: Banker Beware (May 17, 2010), http://www.kirkland.com/siteFiles/Publications/FAEC17D9DF710C8A915E5B457EF6526B.pdf (on file with the *Columbia Law Review*) ("Given the consolidation in the financial services industry and the move away from 'exclusive' banker/client relationships, financial advisory firms often find themselves working opposite their own clients.").

195. See supra notes 175–181 and accompanying text (describing Chancery's rulemaking advantages).

196. See supra notes 185–186 and accompanying text (suggesting SEC may have closer relationship with financial advisors).

tion: codification of Delaware's disclosure rules by the SEC. This solution both retains the advantages of Chancery rulemaking and reduces uncertainty.

A. *SEC Preemption of Delaware Common Law*

The first option is for the SEC to preempt Delaware law by expanding its disclosure rules. The SEC has created national corporate law that displaces state law "via disclosure rules, proxy rules, and general corporate regulation."[197] While it is important to note that SEC preemption of state law is not a common occurrence, the SEC has previously enacted rules for the stated purpose of displacing or reversing Delaware law.[198]

In the context of financial advisor conflicts, the SEC could create a set of disclosure regulations that specifically address the issue. For example, it could propose rules on the requisite extent of contingent fee disclosure and the necessary amount of individual employee disclosure. These proposed rules could then be subject to a statutorily mandated notice-and-comment procedure reinforced by process-based judicial review that has arguably approximated substantive review in recent years.[199] Subjecting disclosure rules to these procedural and substantive protections would result in a more transparent disclosure regime that explicitly considers national interests and cost-benefit analysis.[200] Preemption would also increase uniformity, as dealmakers will only have to look to SEC disclosure rules if Delaware law is no longer valid.

However, unilateral SEC regulations would deny the law the benefit of Chancery decisions. Chancery's experience and specialization in merger law, its flexibility, and its other institutional advantages allow Chancery to make valuable contributions to disclosure law.[201] Both previous and future Chancery decisions add value to SEC disclosure rules because Chancery is exposed to nuanced fact patterns involving contested disclosure issues on a regular basis. While federal preemption may reduce uncertainty, it would eliminate disclosure law innovation

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197. Mark J. Roe, Delaware and Washington as Corporate Lawmakers, 34 Del. J. Corp. L. 1, 11, 23–29 (2009) (describing previous federal preemption of Delaware law in going-private context); see also Roe, Delaware's Competition, supra note 109, at 633–34 (noting how Sarbanes-Oxley Act of 2002 gives SEC power to act to oversee areas of corporate "internal affairs" traditionally left to states).

198. See, e.g., Roe, Delaware's Competition, supra note 109, at 616–21 (noting previous instances in which SEC promulgated rules displacing or directly repudiating Delaware law).

199. See supra Part II.B.1 (describing SEC rulemaking procedure and judicial review of SEC rules).

200. See supra notes 141–144 and accompanying text (describing "economic consequences" test mandated by recent D.C. Circuit opinions).

201. See supra notes 175–181 and accompanying text (describing various institutional advantages of Chancery).

from state experimentation and would rely on the presumption that the SEC is a more capable generator of disclosure law.[202]

B. *SEC Codification of Delaware Decisions*

The preferable method of reconciling the SEC's disclosure mandate and Chancery's increased disclosure activity may be to periodically subject the "rules" created by Chancery's decisions to the SEC's rulemaking process. Codification would likely reduce uncertainty and ensure that all disclosure rules are held to the same rulemaking standards, while still utilizing Chancery's unique competency in corporate law. The SEC likely would not need congressional approval to authorize rules allowing for codification of Delaware disclosure law because it has "virtual[] plenary power to modify and extend the legislative requirements with respect to disclosure."[203] Codifying Delaware's disclosure decisions would be within its broad authority to create disclosure rules.[204]

Codification would build on an avenue of communication between Delaware and the SEC developed in recent years. In 2007, article IV, section 11(8) of the Delaware Constitution was amended to authorize the Delaware Supreme Court to hear and determine questions of Delaware law certified to it by the SEC.[205] The Delaware Supreme Court can choose which questions to certify and stipulate the conditions of certification.[206] In *CA, Inc. v. AFSCME Employees Pension Plan*, the SEC certified two questions of Delaware law to the Delaware Supreme Court,[207] which answered the SEC within three weeks of accepting the questions.[208] Certification avoids inaccurate determinations of Delaware law by the SEC, increasing uniformity for corporations who deal with both the agency and Delaware

202. See, e.g., Roberta Romano, Empowering Investors: A Market Approach to Securities Regulation, 107 Yale L.J. 2359, 2392–95 (1998) (describing how state experimentation leads to useful innovation in corporate law).

203. A.A. Sommer, Jr., Comm'r, Sec. & Exch. Comm'n, Address at the Drexel University Corporate Financial Forecast and Disclosure Conference: Forecasting: A Look at the Future 3 (Mar. 29, 1974), available at https://www.sec.gov/news/speech/1974/032974sommer.pdf (on file with the *Columbia Law Review*). The SEC's plenary power to regulate disclosure is rooted in the Exchange Act. See Securities Exchange Act of 1934, 15 U.S.C. § 78w(a)(1) (2012) (granting SEC power to "make such rules and regulations as may be necessary or appropriate to implement" provisions of Exchange Act).

204. See supra Part II.A (describing SEC's disclosure mandate).

205. 76 Del. Laws 34 (2007) (amending Del. Const. art. IV, § 11(8)).

206. Id.

207. 953 A.2d 227, 229 n.1 (Del. 2008) (noting first instance of SEC certifying questions of Delaware law to Delaware Supreme Court).

208. E.g., Henry duPont Ridgely, Avoiding the Thickets of Guesswork: The Delaware Supreme Court and Certified Questions of Corporation Law, 63 SMU L. Rev. 1127, 1137 (2010) (stating court "accepted the SEC's questions on July 1, heard oral argument on July 9, and issued an opinion on July 17").

courts.[209] SEC codification of Delaware law on disclosure in change-of-control transactions would go a step further in increasing uniformity in corporate law. Codification is similar to the certification process in reverse, with Chancery "submitting" the rules created by its decisions to the SEC rulemaking process. Just as the SEC recognizes that commentary from the Delaware Supreme Court is a valuable method of improving its regulations, Chancery should recognize that the SEC's rulemaking process would strengthen its disclosure rulings.

Codification of Chancery disclosure decisions would subject them to the same rulemaking requirements as proposed SEC regulations. The decisions would have to survive a formalized notice-and-comment procedure that takes into consideration the commentary of parties whose interests may be affected by Chancery decisionmaking but do not have much influence in Delaware litigation.[210] Chancery decisions would also be subject to the same rigorous judicial review and economic cost-benefit analysis by the D.C. Circuit that govern SEC rulemaking.[211] Codification would ensure that if Chancery creates disclosure requirements for the entire set of corporate actors, its rulemaking is held to the same standard as the SEC's.

Codifying Delaware law would also reduce uncertainty for dealmakers. Chancery decisions successfully adopted by the SEC would become federal rules.[212] Actors would be able to look at one set of rules to determine certain disclosure obligations for change-of-control transactions, which would reduce transaction costs.[213] If the SEC did not adopt Chancery decisions, either because the decisions did not survive the public rulemaking process or were challenged and struck down by a court, it would send a strong signal to Chancery to scale back its lawmaking in that area of disclosure law.[214] When federal regulators criticized developments in Delaware law in the past, Delaware courts often reacted by tempering their decisions and even reversing the trajectory of their case law.[215] Thus, even *failure* to successfully codify Chancery deci-

209. See id. at 1133, 1140 (noting other jurisdictions often have to apply Delaware law because so many corporations are incorporated there and arguing certification leads to "more predictable and certain" state law).

210. See supra notes 158–162 and accompanying text (describing differences in interests represented at national level and in Chancery).

211. See supra notes 133–144 and accompanying text (discussing judicial review of SEC rulemaking).

212. See supra Part II.B.1 (discussing SEC rulemaking process).

213. See supra Part II.C (discussing costs of maintaining two sets of disclosure rules). Codification would carry its own transaction costs: The SEC would have to strike a balance between updating disclosure rules and incurring the costs of the rulemaking process too often.

214. Chancery decisions would still be regarded as good Delaware law even if the "rules" were rejected during the codification process.

215. See Roe, Delaware's Competition, supra note 109, at 639–43 (modeling Delaware's case law as reaction to changes in threat of federal intervention over time).

sions on disclosure may result in increased uniformity if Chancery reacts by aligning its jurisprudence more closely with federal rules.[216]

Lastly, codification would leave Chancery with influence over the evolution of disclosure law in change-of-control transactions, preserving its unique institutional advantages and state experimentation generally.[217] Ultimately, harmonizing the two "regulators" would bring to bear the power of a "vigorous duopoly," each with its own unique features,[218] while simultaneously allowing for the standardization of disclosure rules in change-of-control transactions.

CONCLUSION

Congress granted the SEC broad authority to regulate disclosure with the passage of the Exchange Act.[219] In recent years, Chancery has increasingly filled the gaps in broad SEC disclosure regulations, highlighting specific obligations for dealmakers in change-of-control transactions.

Chancery decisions governing the disclosure of financial advisor conflicts provide a useful case study of the substantive and procedural differences in SEC and Chancery rulemaking in an area of significant concern to shareholders considering approving a transaction. The SEC has created broad rules and interpretive guidelines for advisor conflicts of interest while elaborating more concrete disclosure obligations through its staff's comment letters. Chancery has—in dicta and holding—provided substantial guidance on the kinds of financial advisor conflicts with which it is concerned, but the case-specific nature of its opinions has left its doctrine unsettled. The SEC's rules are subject to the informal rulemaking procedures of the APA, and, when challenged, have been increasingly struck down on judicial review. On the other hand, Chancery's unusual "notice-and-comment" process appropriates some of the elements of administrative rulemaking, but its commentary may reflect narrower interest groups and is not reinforced by the requirements of the APA and "hard look" review. Additionally, appellate review of Chancery disclosure decisions is rare and relatively deferential.

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216. See Mark J. Roe, A Spatial Representation of Delaware-Washington Interaction in Corporate Lawmaking, 2012 Colum. Bus. L. Rev. 553, 568–69 (describing Washington and Delaware interaction as possible "two-way street" where Washington's actions influence Delaware and Delaware acts to moderate Washington).

217. See supra notes 175–181 and accompanying text (describing Chancery's unusual institutional advantages).

218. Davidoff, Takeover Regulation, supra note 12, at 268 ("The preservation of Delaware would arguably mitigate risks of SEC industry capture as well as preserve an alternative laboratory for ideas and developments, albeit one subject to SEC supervision and response.").

219. See supra Part II.A (discussing SEC's broad disclosure mandate rooted in Securities Exchange Act of 1934).

The existence of two independent disclosure "regulators" with different sets of substantive rules and rulemaking procedures may have negative implications for dealmakers. First, dealmakers may face increased uncertainty in determining what to disclose. Second, disclosure law may be harmed by the lack of harmonization between two "regulators" with complementary strengths. Chancery is better situated to respond to the rapid pace of change in the transactional market. SEC rulemaking may represent a broader set of interests and is subject to relatively rigorous process-based—and sometimes arguably substantive—judicial review.

The SEC should take action to clarify disclosure rules for the numerous companies subject to both federal and Delaware law. While federal preemption would increase uniformity, SEC codification of Delaware law better incorporates the advantageous rulemaking qualities of each "regulator" while also increasing certainty for dealmakers. In regard to financial advisor conflicts and other areas of importance to shareholders, the costs of parallel disclosure regimes indicate it may be valuable for the SEC and Chancery to collaborate more in their rulemaking.

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