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Do “At-the-Market” Stock Offerings Allow a Board to Comply with Its Duty to Price Stock Issued Under Delaware Law?

The 2013 amendment to Section 152 of the Delaware General Corporation Law allows a board to price securities issuances using a formula, but boards still face risk of non-compliance with their statutory duty to fix the consideration of stock issued in “at-the-market” equity programs.

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In 2013, Section 152 of the Delaware General Corporation Law¹ was amended to clarify that a board of directors may discharge its duty to determine the amount of consideration “for which stock will be issued by approving a formula” to determine the stock price.² Thus, a formula, such

as the average closing market price of the stock over a period of time, may determine the final sale price of the stock. The language in the amendment to Section 152 of the DGCL, referencing a formula to price stock issuances, was borrowed from Section 157(b) of the DGCL, which permits the use of a formula to determine the price of stock options. Some Delaware corporate law commentators have noted that the amendment to Section 152 will facilitate a board’s approval of the issuance of stock or equity programs that determine the price of the stock being issued “at-the-market” or at prevailing market rates.

Since the 2008 financial crisis’ debilitating effect on the financial markets, “at-the-market” (ATM) offerings have become a popular, cost-efficient alternative to large public underwritings for companies to raise capital anonymously over a period of time, and to obtain the best value for the stock at prevailing market prices. In a typical ATM program, the company issuing stock will set parameters for the offering, including a minimum offering price and maximum number of shares to be sold at the discretion of a broker-dealer at the highest prevailing market prices over a prescribed period of time.³

The amendment to Section 152 of the DGCL allows a board to approve stock issuances based on a future market value of stock on a particular day, an average market value over a specified

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time period in the future, or some other formula that would allow calculation of the stock price at a precise or fixed amount in the future. But, in a typical ATM offering, while the broker-dealer is seeking to sell the stock being issued at the highest market price, the stock is sold at the discretion of the broker-dealer at the prevailing market price on any given day during the prescribed period of time, subject to the minimum price set by the board. Thus, the prices in typical ATM offerings are not based on a formula that would establish a fixed stock price in the future, but rather are subject to the fluctuations of the prevailing market prices for the stock over the prescribed period of time. Accordingly, the amendment to Section 152 may not give a board assurance that it has complied with its statutory duty to approve stock issuances priced “at-the-market.”

The Delaware Courts have not yet been asked to decide whether a board complies with its statutory duty when it approves stock issuances priced “at-the-market” with a minimum offering price and maximum number of shares to be sold. Delaware precedent offers no assurance, however, that a board’s duty to determine the price of stock issuances can be discharged by setting a floor or minimum price per share, and then delegating discretion to a broker, banker, or appraiser to depart upwards from the minimum price and fix the precise amount of consideration.⁴ Accordingly, a typical ATM offering could possibly result in uncertainty regarding the authorization of the stock issuance.

There are dire consequences for defectively-issued stock. Defects in the authorization of stock could result in the putative shares being found void and a nullity, which in turn may affect the validity of subsequent corporate acts, even if invalidation would be inequitable.⁵ In 2013, the DGCL was amended to permit ratification of defective corporate acts, and to vest the Delaware Court of Chancery with jurisdiction over matters relating to the cure of defective

corporate acts.⁶ Even with the availability of the self-help remedy to now cure defective corporate acts under the DGCL, the risks and potential liability to issuers, brokers, and investors in ATM offerings for defectively-issued stock are not comforting.

There are, however, two options available under Delaware law to price securities issuances in ATM offerings that provide some assurance that a board has satisfied its statutory duty to determine the price of stock issued under DGCL Section 152. The first option is for the board to form and delegate its power to a committee of the board to approve the price of stock issuances “at-the-market.”⁷ After a broker decides to sell stock at the prevailing market price on any given day, a pricing committee of the board is quickly contacted to perform the perfunctory act of approving the sale price between the broker’s pricing of the sale and the sale’s closing. This first option is both inefficient and impractical.

A typical ATM offering could possibly result in uncertainty regarding the authorization of the stock issuance.

The second option is for the board to approve a maximum and minimum price for stock being issued, and to delegate to a broker to fix the exact price of the stock within the price range determined by the board. Whether this second option would allow a board to comply with its statutory duty to determine the price of stock issuances is, however, unclear under Delaware law. While the Delaware Court of Chancery has suggested that a range of prices or consideration delegated to a broker to fix the exact price of the stock within the range might satisfy a board’s statutory duty, the acceptable size of the price ranges or consideration that would allow a board to fulfill its duty are unclear under Delaware Court of Chancery precedent.⁸

In sum, while ATM offerings are an attractive method for issuers to raise capital in precarious financial markets, the benefits of ATM offerings present difficult issues for a board seeking to ensure compliance with its statutory duty to determine the price of the company's stock.

A Board's Duty to Price Stock Issuances

In requiring strict compliance with statutory formalities when a company issues stock, the Delaware Supreme Court has emphasized that the “issuance of corporate stock is an act of fundamental legal significance having a direct bearing upon questions of corporate governance, control and the capital structure of the enterprise. The law properly requires certainty in such matters.”⁹ Chancellor Strine of the Delaware Court of Chancery has explained that “[t]his mandate is premised on a ‘sensible assumption... the capital structure and ownership of corporations are matters of great importance and should be settled with clarity.’”¹⁰ In the context of determining board compliance with statutory formalities in stock issuances, “law trumps equity.”¹¹

“To ensure certainty, [the Delaware General Corporation Law requires] board approval and a written instrument evidencing the relevant transactions affecting issuance of stock and the corporation's capital structure...”¹² Section 152 of the DGCL requires a board to determine the “‘consideration... for subscriptions to, or the purchase of, the capital stock of a corporation.’”¹³ Thus, in a sale of stock being issued to a purchaser, directors must approve the sale price of the stock.¹⁴ The Delaware Supreme Court has emphasized that “[t]his duty is considered so important that the directors cannot delegate it to the corporation's officers.”¹⁵

The Delaware Courts have not yet been asked to decide whether an ATM stock offering priced “at-the-market” with a minimum offering price and maximum number of shares to be sold complies with the DGCL. Delaware Court precedent

offers no assurance, however, that a board's duty to determine the price of stock can be discharged by setting a floor or minimum price per share, and then delegating to a broker, banker, or appraiser the discretion to depart upwards from the minimum price and fix the sale price for the stock being issued.¹⁶ For example, in the seminal case, *Field v. Carlisle Corp.*, former Vice Chancellor Seitz held that a board's setting an upper limit on the value of property to be received as consideration for the issuance of a company's stock is insufficient to discharge its duty to determine the amount of consideration for the stock issuance. Former Vice Chancellor Seitz reasoned that the company's board improperly had delegated its statutory duty to an appraiser to fix the value of consideration to be received for the company's stock, subject only to the upper limit on value.¹⁷ Similarly, in fulfilling its duty to fix the consideration in a merger under DGCL Section 251(b), a board may not set a floor or minimum price per share, and then delegate to an investment banker or financial advisor the discretion to fix the merger price, subject only to the floor or minimum price.¹⁸

Thus, the typical ATM offering, in which a broker sells stock being issued at the prevailing market price subject to the minimum price set by the board, may possibly not comply with a board's duty to price stock issuances under DGCL Section 152. If stock is invalidly issued, the putative shares may be void and treated as a nullity for purposes of validating subsequent corporate acts¹⁹—if not ratified by the self-help remedy for defective corporate acts in new DGCL Section 204, or validated by the Court of Chancery under new DGCL Section 205.

DGCL Section 152 was amended in 2013 to clarify that a board may determine the price of a stock issuance by using a formula. Some Delaware corporate law commentators have noted that this amendment will help boards price securities issued in ATM offerings in compliance with their statutory duty under Section 152.²⁰ But, since

the prices in typical ATM offerings are not based on a formula that would establish a fixed stock price in the future, the amendment does not go far enough to expressly allow a board to set a floor or minimum price in an ATM offering, and then delegate to a broker the discretion to depart upwards from the minimum price and fix the sale price based on an actual trade at a future prevailing market price.

Options for Board to Price Securities Issuances in ATM Offerings

Two options are available under Delaware law that provide some assurance that a board has complied with its duty to price securities issued in ATM offerings under DGCL Section 152. In the first option, a board approves the price of the shares sold in the ATM offering. Since the process of securing approval from the whole board of the stock price after a broker decides to sell stock at the prevailing market price on any given day is impractical, the board is advised to form and delegate its power to a committee of the board to approve the price of stock issuances in the ATM offering.²¹ In short, between the time that the broker decides to sell stock at the prevailing market price and the closing of the sale, a properly-authorized committee of the board would quickly execute a written consent approving a schedule of the sales on any given day.

The acceptable size of the price ranges or consideration that would allow a board to satisfy its statutory duty is unclear.

In addition to being inefficient, the pricing committee's act of approving the sale price between the broker's pricing of the sale and the sale's closing often is merely perfunctory due to the relatively limited time available for the committee to consider the sufficiency of the price of

the stock being sold before the closing of the sale in an ATM offering. Thus, while providing technical compliance with a board's statutory duty to determine the price of the stock issuance, query whether the committee's perfunctory approval of the sale price serves the salutary Delaware corporate law policies, underlying a board's duty to determine the value of consideration in a stock issuance.²² Moreover, since the putative shares are not validly issued under DGCL Section 152 until the committee approves the sale price, corporate issuers can only give qualified opinions that the putative shares being sold will be valid upon the committee's future authorization to issue the shares at the sale price in the ATM offering. Qualified opinions from an issuer concerning the validity of the issuance of its stock expose broker-dealers selling the stock in ATM offerings to greater risk of liability.

The second option is for the board to approve a maximum and minimum price for stock being issued, and to delegate to a broker to fix the exact price of the stock within the price range determined by the board. Since no Delaware Court has yet ruled that a price range or range of consideration discharges a board's statutory duty to determine the price of stock issued under DGCL Section 152, whether this second option would allow a board to comply with its statutory duty is unclear. But, Delaware case-law authorities, as well as the language of Section 152 itself, authorizing issuances for an amount of "consideration" (e.g., which language does not limit the amount of consideration to a precise or exact price) suggest that a range of consideration delegated to a broker to fix the exact price of the stock "at-the-market" within the range might satisfy a board's statutory duty under DGCL Section 152.²³

Further, the acceptable size of the price ranges or consideration that would allow a board to satisfy its statutory duty under DGCL Section 152 also is unclear. The Delaware Court of Chancery, however, has provided some guidance to help a board determine an acceptable price range for

stock issuances.²⁴ While these guidelines do not provide a precise formula for acceptable ranges of consideration, they suggest that the smaller the range of consideration (based on the quantity of shares being issued multiplied by the range differential between the minimum and maximum price-per-share) and the larger a company's size or capitalization, the more likely that a board's determination of a range of consideration for an issuance of stock will satisfy its duty under DGCL Section 152.²⁵ In short, the smaller the price range or range of consideration and the larger the size of the company, the less likely that the spread in the price range will be significant, or of "real substance," mandating that a board consider the exact or precise price within the range under Section 152.²⁶

Consideration should be given as to whether further amendment to Section 152 of the DGCL is appropriate.

In sum, the options available to a board seeking to ensure compliance with its duty to price securities issued in ATM offerings are either impractical, or of uncertain validity. Due to the limitations in these options and the rise in popularity of ATM offerings in response to the chaos in the financial markets, consideration should be given as to whether further amendment to Section 152 of the DGCL is appropriate to expressly permit board compliance with its statutory duty to determine the price of stock in ATM offerings.

Amendment of Section 152 to Facilitate ATM Offerings

One school of thought counsels against further amendment to Section 152 of the DGCL to facilitate a board's compliance with its statutory duty to determine the price of stock in ATM offerings. This school of thought reasons that longstanding Delaware case law, interpreting

Section 152 and its statutory predecessors to require that a board of directors determine the amount of consideration for corporate stock issuances, is premised on acts of fundamental legal significance concerning the company's capital structure, control, and good corporate governance. Thus, capital structure and ownership of corporations are matters so fundamental to corporate control and governance that they must be settled by a board and with clarity under Delaware corporate law. As former Vice Chancellor Seitz emphasized in *Field*, while a board may employ financial advisors to help the board determine the amount of consideration to be received for issuance of the company's stock, these advisors are employed to aid the directors, but the board's discretion is not delegated to the financial advisors; instead, the final determination of the value of the consideration remains with the directors.²⁷

Another school of thought posits, however, that further amendment of Section 152 to accommodate ATM offerings would comport with Delaware corporate law policies and is necessary to keep Delaware at the forefront of corporate law and the State of first choice for incorporation. ATM offerings continue to increase in popularity as an alternative to public underwritings for a company to raise capital anonymously and at the highest prevailing market prices in order to obtain the best value for its stock issuances and raise the most capital for its needs.

While facilitating a board's compliance with its statutory duty to determine the price of stock in ATM offerings may not be the determinative factor in deciding where to incorporate, faced with aggressive competition from other states to usurp the Delaware corporate law franchise, the ability to ensure that stock is issued validly in ATM offerings is certainly a factor to consider in the decision where to incorporate today. Indeed, Illinois, Maryland, New Mexico, and Pennsylvania have corporate statutes that expressly validate the issuance of shares in a typical ATM offering, in

which the board sets a minimum offering price and maximum number of shares to be sold at the highest prevailing market prices over a prescribed period of time.²⁸

The final determination of the value of the consideration remains with the directors.

Moreover, query whether a typical ATM offering undermines Delaware corporate law policies. When a board with the aid of its financial advisors has determined a minimum price or range of consideration that is acceptable to the board for a stock issuance to raise necessary capital, and then delegates to a broker to sell the stock at the highest prevailing market price above the minimum or within the range of consideration in order to obtain the best value for the company's stock, has not the board fulfilled its duty to maximize value in the company's capital structure, and met the interests of both the company and its existing shareholders? Indeed, an ATM offering allows the company the opportunity to obtain the highest price for its stock, raising the most capital to meet the company's requirements, while having the least dilutive effect on the value of the stock of existing shareholders. Finally, in comparing a pricing committee's perfunctory approval of a sale price between a broker's pricing of the sale and the sale's closing in an ATM offering, which option presently is being recommended by some Delaware counsel to ensure technical compliance with a board's statutory duty to determine the price of a stock issuance, the above method of board approval of a minimum price or range of consideration with the aid of financial advisors is more true to actually serving the salutary Delaware corporate law policies.

Conclusion

In sum, ATM offerings are an increasingly popular method for issuers to maximize their

ability to obtain the best value for their stock in precarious financial markets while raising the most capital to meet their requirements. But, even with the 2013 amendment to Section 152 of the Delaware General Corporation Law, which allows boards to price securities issuances using a formula, ATM offerings continue to present difficult issues for a board seeking to ensure certainty regarding its compliance with its statutory duty to determine the amount of consideration to be received for stock issuances.

The board-pricing-committee and range-of-consideration options available to a board seeking to ensure compliance with its duty to price securities issuances in ATM offerings under Delaware law are impractical, inefficient, or of uncertain validity. Accordingly, due to the limitations in these options and the rise in popularity of ATM offerings, further amendment of Section 152 to expressly permit board compliance with its duty to price securities issuances in ATM offerings is warranted to maintain Delaware's preeminence in the corporate law arena.

Notes

1. Delaware General Corporation Law is hereinafter referred to as DGCL.
2. H.B. 127, 147th General Assembly 13, 79 Del. Laws, ch. 72, Section 3 (2013) (comment in legislative synopsis to amendment to DGCL Section 152). The amendment adds the following sentence to Section 152 of the DGCL: "The board of directors may determine the amount of such consideration by approving a formula by which the amount of consideration is determined." 8 *Del. C.* Section 152.
3. Barbara J. Endres & Kersti Hanson, *At-the-Market Offerings-Implications of Regulation M*, 43 *Rev. Sec. & Commodities Reg.* 1, 2 (2010). At-the-market offerings must comply with the requirements of Rule 415(a)(iv) under the Securities Act of 1933.
4. *OmniOffices, Inc. v. Kaidanow*, 2001 WL 1701683, at *11 (D.D.C. Sept. 12, 2001) (summary of Delaware cases, ruling that board may not satisfy its statutory duty to determine the price of its stock by setting a floor or minimum price per share, and delegating discretion to a third party to depart upwards to determine the precise amount of consideration for the stock being issued), *rev'd on other grounds*, 321 F.3d 165 (D.C. Cir. 2003).

5. *STAAR Surgical Co. v. Waggoner*, 588 A.2d 1130, 1136-37 (Del. 1991).
6. 8 *Del. C.* Sections 204, 205. H.B. 127, 147th General Assembly 13, 79 *Del. Laws*, ch. 72, Sections 4, 5 (2013) (legislative synopsis to amendment to DGCL Section 204 provides that “‘defective corporate acts’ and ‘putative stock’ shall not be void or voidable solely due to a ‘failure of authorization’, if ratified as provided in Section 204 or if validated by the Court of Chancery in a proceeding pursuant to new Section 205. Section 204 is intended to overturn the holdings in case law, such as *STAAR Surgical Co. v. Waggoner*, 588 A.2d 1130 (Del. 1991) and *Blades v. Wischart*, 2010 WL 4638603 (Del. Ch. Nov. 17, 2010), that corporate acts or transactions and stock found to be ‘void’ due to a failure to comply with the applicable provisions of the General Corporation Law or the corporation’s organizational documents may not be ratified or otherwise validated on equitable grounds.”).
7. See John Mark Zeberkiewicz & Tiffany N. Piland, *Valid Issuance of Capital Stock*, 44 *Rev. Sec. & Commodities Reg.* 191, 196 (2011) (citing 8 *Del. C.* Section 141(c)).
8. See *Field v. Carlisle Corp.*, 68 A.2d 817, 821 (Del. Ch. 1949) (Seitz, V.C.).
9. *Grimes v. Alteon Inc.*, 804 A.2d 256, 261 (Del. 2002) (quoting *STAAR Surgical Co. v. Waggoner*, 588 A.2d 1130, 1136 (Del. 1991)).
10. *Blades v. Wischart*, 2010 WL 4638603, at *10 (Del. Ch. Nov. 17, 2010) (quoting *Liebermann v. Frangiosa*, 844 A.2d 992 1004 (Del. Ch. 2002)), *aff’d sub nom. Wetzel v. Blades*, 35 A.3d 420 (Del. 2011) (TABLE).
11. *Blades v. Wischart*, 2010 WL 4638603, at *10 (Del. Ch. Nov. 17, 2010) (citing *STAAR Surgical Co. v. Waggoner*, 588 A.2d 1130 (Del. 1991)), *aff’d sub nom. Wetzel v. Blades*, 35 A.3d 420 (Del. 2011) (TABLE), *but see* 8 *Del. C.* Section 204(a) (In 2013, the DGCL was amended to provide a self-help remedy: “no defective corporate act or putative stock shall be void or voidable solely as a result of a failure of authorization if ratified as provided in this section or validated by the Court of Chancery in a proceeding brought under Section 205 of this title”).
12. *Grimes v. Alteon Inc.*, 804 A.2d 256, 261 (Del. 2002).
13. *Id.* (quoting 8 *Del. C.* Section 152); *Olson v. EV3, Inc.*, 2011 WL 704409, at *12-13 (Del. Ch. Feb. 21, 2011) (“longstanding Delaware case law interpreting Section 152 and its statutory predecessors requires that the board of directors determine the sufficiency of the consideration received for shares”).
14. *Grimes*, 804 A.2d at 261 (citing *Field v. Carlisle Corp.*, 68 A.2d 817, 818 (Del. Ch. 1949)).
15. *Id.* (citing *Field*, 68 A.2d at 818).
16. *Omnioffices, Inc. v. Kaidanow*, 2001 WL 1701683, at *11 (D.D.C. Sept. 12, 2001) (summary of Delaware case law that a “board’s statutory duty to determine the price of its stock is not discharged by setting floor price per share”), *rev’d on other grounds*, 321 F.3d 165 (D.C. Cir. 2003); *see also Aveta Inc. v. Cavallieri*, 23 A.3d 157, 178 (Del. Ch. 2010) (setting a “dubious floor price and delegate[ing] to a financial advisor unfettered discretion to depart upwards” to fix the merger price for the stock of a company is an improper delegation of board authority).
17. *Field v. Carlisle Corp.*, 68 A.2d 817, 820-21 (Del. Ch. 1949) (Seitz, V.C.).
18. *Jackson v. Turnbull*, 1994 Del. Ch. WL 174668, at *4-5 (Del. Ch. Feb. 8, 1994), *aff’d*, 653 A.2d 306 (Del. 1994) (TABLE); *see also Clark Mem’l College v. Monaghan Land Co.*, 257 A.2d 234, 241 (Del. Ch. 1969) (directors setting minimum sale price for company’s assets, and delegating to company’s officers authority to fix terms and conditions of the sale, including the sale price of the assets, was an improper delegation of authority conferred on the board by the stockholders’ resolution empowering the sale of the company’s assets under DGCL Section 271(a)).
19. *STAAR Surgical Co. v. Waggoner*, 588 A.2d 1130, 1136-37 (Del. 1991).
20. See, e.g., John F. Grossbauer and Mark A. Morton, *2013 Amendments to the Delaware General Corporation Law*, 1, 7 (July 26, 2013), available at http://www.potteranderson.com/uploads/1183/doc/2013_Amendments_to_the_DGGL_July_2013.pdf (Section 152 “expressly permits the board of directors of a Delaware corporation to determine the amount of consideration by using a formula. This will facilitate pricing of securities issuances ‘at the market.’”).
21. See John Mark Zeberkiewicz & Tiffany N. Piland, *Valid Issuance of Capital Stock*, 44 *Rev. Sec. & Commodities Reg.* 191, 196 (2011) (citing 8 *Del. C.* Section 141(c)).
22. See *Grimes v. Alteon Inc.*, 804 A.2d 256, 261 (Del. 2002) (quoting *STAAR Surgical Co. v. Waggoner*, 588 A.2d 1130, 1136 (Del. 1991)).
23. *Field v. Carlisle Corp.*, 68 A.2d 817, 821 (Del. Ch. 1949) (Seitz, V.C.); *Omnioffices, Inc. v. Kaidanow*, 2001 WL 1701683, at *10 (D.D.C. Sept. 12, 2001), *rev’d on other grounds*, 321 F.3d 165 (D.C. Cir. 2003).
24. See *Field*, 68 A.2d at 821.
25. See *Field*, 68 A.2d at 821; *Omnioffices*, 2001 WL 1701683, at *10.
26. The following sample board resolution approves a range of consideration, incorporating a formula, that may be effective to discharge a board’s statutory duty under Section 152 of the DGCL:
The Board of _____ (the “Company”) hereby authorizes the issuance of [QUANTITY] shares of the Company’s common stock, par value 0.001 per share, for an amount of consideration to be determined in accordance with the following formula:

The Board authorizes [broker] to sell up to [QUANTITY] shares of the Company’s common stock, par value 0.001 per share, at or

above a minimum market price equal to $\$ X - ((5\% \text{ of } X) \text{ or } \$ Y$ per share) and at or below a maximum market price equal to $\$ X + ((20\% \text{ of } X) \text{ or } \$ Z$ per share) with X being the closing trade price per share on [DATE]. Sales should begin on or after the date of this Resolution, and shall continue until [DATE] [or to when all issued shares are sold].

27. *Field v. Carlisle Corp.*, 68 A.2d 817, 820 (Del. Ch. 1949) (Seitz, V.C.) (citing statutory predecessor to 8 *Del. C.* Section 141(e) which gives directors protection for their determination of the value of consideration when they rely upon the report of a financial advisor, appraiser, or other expert). Moreover, if Section 152 is amended to facilitate a board's compliance with its duty to price securities issuances in ATM offerings, query whether amendment of the Delaware General Corporation Law regarding the pricing of stock options (8 *Del. C.* Section 157(b)), rights and designations in classes and series of stock (8 *Del. C.*

Section 151(a)), and board determinations of consideration for mergers and other acquisitions (8 *Del. C.* Section 251(b)) also would now be required?

28. See 805 ILL. Comp. Stat. 5/6.25(a) (board may price stock being issued by establishing "a minimum price or a general formula or method by which the price can be determined"); MD Code Ann., Corporations and Associations, Section 2-203(a)(2) (board may price stock being issued by setting "the minimum consideration for the stock... or a formula for its determination"); N.M. Stat. Section 53-11-18A (board may price stock being issued by establishing "a minimum price or general formula or method by which the price will be determined"); 15 Pa. C.S.A. Section 1523 (an officer may determine, "within limits, pursuant to a formula or method or subject to relevant criteria specifically prescribed by the board... price or consideration and other terms on which shares will be issued").

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