

## Delaware Chancery Court: Applies *Rales* as General Demand Futility Test Largely Sidelining *Aronson*

11.23.20



(Article from *Securities Law Alert*, November 2020)

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On October 26, 2020, the Delaware Chancery Court dismissed a derivative action, related to an abandoned stock reclassification plan, against current and former directors of Facebook because plaintiff did not make a pre-suit demand and failed to establish demand futility. [United Food & Com. Workers Union & Participating Food Indus. Emps. Tri-State Pension Fund v. Zuckerberg](#), 2020 WL 6266162 (Del. Ch. 2020) (Laster, V.C.). The court held that it would apply *Rales v. Blasband*, 634 A.2d 927 (Del. 1993) as the general demand futility test.

### ***The Court Weighs the Two Demand Futility Tests Against Each Other***

The court began its analysis by comparing the two demand futility tests the Delaware Supreme Court has established which are found in *Rales* and in *Aronson v. Lewis*, 473 A.2d 805 (Del. 1984). The court observed that “the *Aronson* test has proved to be comparatively narrow and inflexible in its application, and its formulation has not fared well in the face of subsequent judicial developments.” Whereas, “[t]he *Rales* test, by contrast, has proved to be broad and flexible, and it encompasses the *Aronson* test as a special case.”

### ***The Court Points Out the Limitations of Aronson***

Pointing out the weakness of *Aronson* as applied to the facts in this case, the court stated that “*Aronson* does not provide guidance about what to do with either the director who abstained [from the vote on the reclassification] or the two directors who joined the Board later.” The court continued that “[t]he director who abstained from voting on the Reclassification suffers from other conflicts that renders her incapable of considering a demand, yet a strict reading of *Aronson* only focuses on the challenged decision and therefore would not account for those conflicts.” Further, the court pointed out that “the plaintiff alleges that one of the directors who subsequently joined the Board has conflicts that render him incapable of considering a demand, but a strict reading of *Aronson* would not account for that either.”

### ***The Court Applies Rales as General Demand Futility Test***

The court concluded that “[p]recedent thus calls for applying *Aronson*, but its analytical framework is not up to the task. The *Rales* test, by contrast, can accommodate all of these considerations.” The court then announced that “[t]his decision therefore applies *Rales* as the general demand futility test.” The court explained that it would draw “upon *Aronson*-like principles when evaluating whether particular directors face

a substantial likelihood of liability as a result of having participated in the decision to approve the Reclassification.”

The court stated that it would proceed “on a director-by-director basis, asking for each director (i) whether the director received a material personal benefit from the alleged misconduct that is the subject of the litigation demand, (ii) whether the director would face a substantial likelihood of liability on any of the claims that are the subject of the litigation demand, and (iii) whether the director lacks independence from someone who received a material personal benefit from the alleged misconduct that is the subject of the litigation demand or who would face a substantial likelihood of liability on any of the claims that are the subject of the litigation demand.”

Reviewing the facts concerning the directors who were on the board when the complaint was filed, the court considered whether they validly could consider a litigation demand. Finding a majority would be disinterested, independent, and capable of considering a litigation demand, the court held that demand was not excused and granted defendants’ motion to dismiss.

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