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MORRIS NICHOLS ARSHT & TUNNELL

Delaware Supreme Court Interprets Private Company Voting Agreement that Departs from Standard NVCA Voting Terms

For reasons of economy in an early-stage investment, venture capitalists and founders often will use forms made available by the National Venture Capital Association (NVCA) as a basis to negotiate the post-investment governance structure of a corporation. In *Salamone v. Gorman*, the Delaware Supreme Court interpreted the product of such a negotiation. As noted in the opinion, the NVCA form contemplates *per share* (and not *per capita*) voting, and the opinion is a reminder of the need for clarity if there is intent to depart from such a regime.

Salamone involved a voting agreement entered into in connection with an approximate $7,400,000 Series A round of financing of Westech Capital Corporation. Although the parties used the NVCA form voting agreement as a basis to set out the post-investment board composition, they made three key departures. First, with respect to a "Series A Designee," the NVCA form language "the holders of a majority of the Shares" was changed to "the majority of the holders of the Series A Preferred Stock." Second, with respect to the "Key Holder Designees," the NVCA form language was changed from "one individual designated by the holders of a majority of the shares" to "two persons elected by the Key Holders." Finally, with respect to the "Independent Designees," the NVCA form language "mutually acceptable to (i) the holders of a majority of the Shares held by the Key Holders . . . and (ii) the holders of a majority of the Shares held by the Investors" was changed to "Independent Directors mutually acceptable to the Series A Designees and the Key Holder Designees of the Board."

When a dispute arose between two camps of stockholders, one camp argued that the literal terms of the voting agreement required that each of the Series A Designee, Key Holder Designees and Independent Designees was nominated *per capita* (i.e., that each holder had one vote regardless of the number of shares they owned); the other camp argued that each such Designee was nominated *per share*. Prior to interpreting the provisions, the Court provided the following guidelines:

- If a Court is interpreting the voting provisions of a *certificate of incorporation*, a presumption against *per capita* voting will apply if the certificate is not clear on its face.
- If a Court is interpreting the voting provisions of a voting agreement (as in this case), the Court will first consider parol evidence to clarify any ambiguity. If "the trial court finds by clear and convincing evidence" that the parties contemplated *per capita* voting, it can rule for the party arguing for such a structure. "When, however, the parol evidence does not rise to that level and leaves the trial court without the requisite level of certainty, the presumption against disenfranchisement requires reading the contract consistent with" *per share* voting.

With these principles in mind, the Court held that the Key Holder Designees and Independent Designees are both nominated and removable on a *per capita* basis. Although the Court found the voting requirement for the Series A Designee "particularly close" (in fact, the Court stated it may have interpreted the contract differently if it were the trial court in the first instance), the Supreme Court affirmed the Court of Chancery's determination that the provision was ambiguous in light of the entirety of the voting agreement provisions, and that there was not "clear and convincing" evidence to overcome the presumption against *per capita* voting. Accordingly, the Court held that the Series A Designee was nominated on a *per share* basis.

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