

Practice Update

Delaware Supreme Court Decision Creates New Paradigm for Derivative Claims

September 24, 2021

On September 23, the Delaware Supreme Court issued a decision replacing the long-standing *Aronson* test for demand futility and instead adopts and affirms a new universal *Rales*-like test applied below by Vice Chancellor Laster as follows:

From this point forward, courts should ask the following three questions on a director-by-director basis when evaluating allegations of demand futility:

1. Did the director receive a material personal benefit from the alleged misconduct that is the subject of the litigation demand?
2. Does the director face a substantial likelihood of liability on any of the claims that would be the subject of the litigation demand?
3. Does the director lack independence from someone who received a material personal benefit from the alleged misconduct that would be 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?

If the answer to any of the questions is “yes” for at least half of the members of the demand board, then demand is excused as futile. It is no longer necessary to determine whether the *Aronson* test or the *Rales*

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test governs a complaint's demand-futility allegations.

As the Court explained: “This approach treat[s] *Rales* as the general demand futility test, while drawing 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 [transaction].” *Rales* is more flexible and arguably broader than *Aronson*, focusing on the decision regarding the litigation demand rather than the transaction being challenged.

Substantively, this is not a major departure from existing principles and the Court made clear that cases applying *Aronson* and *Rales* remain good law. However, the re-articulated test is a new paradigm for derivative claims that will likely make its way to other courts around the country over time (as *Aronson* did in many states).

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