DExit and Texas: Race to the Top

SUMMARY OF SELECTED DISTINCTIONS BETWEEN TEXAS AND DELAWARE CORPORATE LAW AND CERTAIN RELATED MATTERS EFFECTIVE SEPTEMBER 1, 2025

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INTERNAL AFFAIRS DOCTRINE, CHOICE OF LAW AND FORUM:

"The internal affairs doctrine is a conflict of laws principle which recognizes that only one State should have the authority to regulate a corporation's internal affairs." *Edgar v. MITE Corp.*, 457 U.S. 624, 645 (1982). "[U]nder the commerce clause a state has no interest in regulating the internal affairs of foreign corporations." *McDermott, Inc. v. Lewis*, 531 A.2d 206, 217 (Del. 1987) (internal quotations omitted); Frederick Tung, *Before Competition: Origins of the Internal Affairs Doctrine*, 32 J. Corp. L. 33, 39 (Fall 2006).

Both Delaware and Texas subscribe to the internal affairs doctrine which provides that "the law of the state of organization of an entity governs its internal affairs, including the liability of an owner or governing person of the entity for actions taken in that capacity." EGAN ON ENTITIES: Corporations, Partnerships and Limited Liability Companies in Texas (4th Ed. 2023) ("EGAN ON ENTITIES"), § 2.6.2 (citing the Texas Business Organizations Code ("TBOC") §§ 1.101-1.105; *see JUUL Labs, Inc. v. Grove*, C.A. No. 2020-0005-JTL (Del. Ch. Aug. 13, 2020); *VantagePoint Venture Partners 1996 v. Examen, Inc.*, 871 A.2d 1108, 1115-1118 (Del. 2005); *see also Klinek v. LuxeYard, Inc.*, 596 S.W.3d 437, 446-48 (Tex. App. – Houston [14th Dist.], pet. filed April 27, 2020).

In Texas, a corporation, partnership and limited liability company ("LLC") may include a provision in its governing documents (certificate of formation and bylaws) that chooses a Texas court as the exclusive forum and venue, and prospectively waives jury trials, for internal entity claims enforceable even if not signed by the person to be bound thereby. TBOC §§ 2.115 and 2.116.

In Delaware, a corporation may have a charter or bylaw forum selection clause in its governing documents that applies not only to "internal corporate claims" but also to claims that "relate to the business of the corporation, the conduct of its affairs, or the rights or powers of the corporation or its stockholders, directors or officers"—so long as at least one Delaware state or federal court remains available as a forum, consistent with applicable jurisdictional requirements. A forum selection provision addressing non-internal corporate claims cannot prohibit claims from being brought in a court in Delaware "that has jurisdiction over such claims." DGCL § 115. The Delaware Court of Chancery is a court of equity which does not have jury trials.

SELECTED GOVERNANCE PRINCIPLES:

	Texas	**Delaware**
Fiduciary Duties	Texas has its own body of jurisprudence for fiduciary duties and in one of the seminal cases of director fiduciary duties under Texas law, the U.S. Court of Appeals for the Fifth Circuit criticized the parties' arguments based on Delaware cases and their failure to cite Texas law in briefing on director of fiduciary duties. Fiduciary duties are owed to the corporation. Directors may consider long term and short term interests of the corporation and shareholders, including whether those interests may be best served by the continued independence of the corporation. *See* EGAN ON ENTITIES, § 2.6.3 (citing and quoting *Gearhart Indus., Inc. v. Smith Int'l*, 741 F.2d 707, 719 n. 4 (5th Cir. 1984)). Under Texas law "[a] director's fiduciary status creates three broad duties: duties of obedience, loyalty, and due care." *In re Estate of Poe*, 648 S.W.3d 277, 290 (2022) (citing *Loy v. Harter*, 128 S.W.3d 397, 407 (Tex. App. – Texarkana 2004, pet denied (citing *Gearhart*, 741 F.2d at 719-721 (5th Cir. 1984))). The *Gearhart* court commented that: (i) the duty of obedience requires a director to avoid committing *ultra vires* acts, i.e., acts beyond the scope of the authority of the corporation as defined by its articles of incorporation or the laws of the state of incorporation, (ii) the duty of loyalty dictates that a director must act in good faith and must not allow his personal interests to prevail over the interests of the corporation, and (iii) the duty of due care requires that a director must handle his corporate duties with such care as an ordinarily prudent man would use under similar circumstances. EGAN ON ENTITIES, § 2.6.3 (citing *Gearhart*, 741 F.2d at 719-721). TBOC § 1.056 provides that managerial officials of a Texas corporation may, but are not required to, consider the laws, judicial decisions, or business practices of other states in exercising their powers and that a failure to consider or conform to such out-of-state authorities does not constitute or imply a breach of the TBOC or any duty under Texas law.	The principal fiduciary duties under Delaware law are (1) the duty of loyalty and (2) the duty of care. Fiduciary duties are owed to the corporation and its stockholders. EGAN ON ENTITIES § 2.6.4. In *Revlon, Inc. v. MacAndrews & Forbes, Inc.*, 506 A.2d 173 (Del. 1986) the Delaware Supreme Court held that directors have a duty to seek the highest value obtainable when a sale of the company becomes inevitable. EGAN ON ENTITIES § 2.6.13(b)(2)(ii).

	Texas	Delaware
	TBOC § 1.057 provides that (i) directors and officers of a Texas corporation may, but are not required to, consider the laws, judicial decisions or business practices of other states in exercising their powers and that a failure to consider or conform to such out-of-state authorities does not constitute or imply a breach of the TBOC or any duty under Texas law and (ii) the provisions of the TBOC may not be supplanted, contravened or modified by the laws or judicial decisions of another state.	
Duty of Obedience	A breach of the duty of obedience occurs when directors commit "*ultra vires acts*, i.e., acts beyond the scope of the powers of the corporation as defined by its articles of incorporation and Texas law." EGAN ON ENTITIES, § 2.6.3(c)(1) (citing *Gearhart*, 741 F.2d at 719.).	No separate and distinct fiduciary duty of obedience under Delaware law, but the concept is embedded elsewhere in the Delaware fiduciary duties. EGAN ON ENTITIES § 2.6.4.
Duty of Loyalty	The duty of loyalty in Texas is a duty that dictates that the director act in good faith and not allow his or her personal interest to prevail over that of the corporation. *Gearhart*, 741 F.2d at 719. "The duty of loyalty dictates that a corporate officer or director must act in good faith and must not allow his or her personal interest to prevail over the interest of the corporation. The duty of loyalty is described as requiring an extreme measure of candor, unselfishness, and good faith on the part of the officer or director." *Loy v. Harter*, 128 S.W.3d 397, 407 (Tex. App. – Texarkana 2004, pet. denied) (citing *Holloway*, 368 S.W.2d at 577. <u>Good Faith</u>: "Good faith" has been held to mean "[a] state of mind consisting in (1) honesty of belief or purpose, (2) faithfulness to one's duty or obligation, . . . or (4) absence of intent to defraud or to seek unconscionable advantage." *Johnson v. Jackson Walker, L.L.P.*, 247 S.W.3d 765, 772 (Tex. App. –	"[T]he duty of loyalty is transgressed when a corporate fiduciary, whether director, officer or controlling shareholder, uses his or her corporate office or, in the case of a controlling shareholder, control over corporate machinery, to promote, advance or effectuate a transaction between the corporation and such person (or an entity in which the fiduciary has a substantial economic interest, directly or indirectly) and that transaction is not substantively fair to the corporation. That is, breach of loyalty cases inevitably involve conflicting economic or other interests, even if only in the somewhat diluted form present in every "entrenchment" case." *Solash v. Telex Corp.*, No. 9518, 9528, 9525, 1988 WL 3587, at *7, 1988 Del. Ch. LEXIS 7, at *19-*20 (Del. Ch. Jan. 19, 1988). <u>Good Faith</u>: Under Delaware law, "the fiduciary duty of loyalty is not limited to cases involving a financial or other cognizable fiduciary conflict of interest", rather it arises in the context of the failure to act in good faith. *See Stone v. Ritter*, 911 A.2d 362, 370 (Del. 2006).

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