

April 24, 2018

Approval of Enhanced Advance Notice Bylaws

On April 3, 2018, the Superior Court of Washington for King County issued a decision affirming the use of enhanced advance notice bylaws and finding that the board's decision to reject a deficient notice is an exercise of its business judgment. The case is *Blue Lion Opportunity Master Fund, L.P. vs. HomeStreet, Inc.*, No. 18-2-06791-0 SEA. While this is a Washington state decision, it was widely followed as Delaware courts have not yet addressed the validity of enhanced advance notice bylaws. The case is also a reminder of the importance of well-drafted advance notice bylaws, which can serve as an effective first line of defense to a hostile proxy contest. Likewise, shareholders seeking to nominate candidates should carefully review the target company's advance notice bylaws to ensure that its notice satisfies every procedural requirement, no matter how trivial.

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HomeStreet is a financial services corporation based in Washington. HomeStreet's advance notice bylaws require that any notice submission include extensive information regarding the candidate's background and qualifications, including a 52-page questionnaire, as well as any other information required to be disclosed in a proxy statement by incorporating by reference extensive SEC regulations. Blue Lion Capital ("BLC"), a hedge fund, delivered a 133-page notice the day before the advance notice deadline.

On February 23, BLC delivered a notice letter (the "Notice Letter") to the board—the day before the Company's advance notice deadline. The Notice Letter informed the board of BLC's intention to nominate two independent directors, and to submit two substantive corporate governance proposals.

BLC and HomeStreet both subsequently embarked on public "letter campaigns" to defend their positions. On March 1—six days after receiving BLC's notice—the board issued a press release announcing that it had rejected BLC's Notice Letter as invalid. HomeStreet identified "at least 32 instances of failures to satisfy the requirements set forth in the bylaws."¹ For example, the board found that the Notice Letter failed to provide information required under the bylaws by reference to the federal proxy rules, such as BLC's estimated proxy fight cost and whether BLC planned to seek reimbursement from the Company, and failed to include information regarding share ownership of BLC affiliates. BLC sought to cure the alleged deficiencies in a supplemental submission, which the board rejected as untimely.

In response, BLC issued press releases defending the validity of its 133-page Notice Letter and denouncing the board's decision as self-interested and in "bad faith." As an example, BLC noted that the board did not reject the Notice Letter on the grounds that it did not have sufficient knowledge of BLC's intended actions, but rather that the Notice Letter failed to comply with several procedural technicalities that the board disingenuously read into the bylaws.²

¹ HomeStreet Press Release, *HomeStreet Discloses That Notice of Director Nominations and Proposals from Blue Lion Capital is Invalid*, March 1, 2018, available [here](#).

² "Nowhere in its objection to BLC's Notice does HomeStreet claim it has insufficient knowledge of BLC's intended actions. Instead, HomeStreet's Board attempts to invalidate the Notice with a novel objection: BLC not only needed to provide the information required (which it did), but BLC also needed to repeat "No Further Information" or "Not Applicable" more than twenty-five times, to confirm that there was nothing else it needed to disclose." BLC Press Release, *HomeStreet Board Reveals Disdain for Shareholder Rights*, March 8, 2018, available [here](#).

On March 13, BLC filed a complaint against the Company in Washington state court, seeking a declaratory judgment that the Notice Letter complied with the Company's bylaw requirements, and moved to enjoin the Company from rejecting the Notice Letter as invalid. BLC argued that enhanced scrutiny should apply to the board's decision and that the bylaw should be struck down because it "unduly restrict[s] the stockholder franchise." Compl., ¶ 78. On April 3, the court held that the Company's advance notice bylaw was valid and that BLC had failed to comply with its requirements. The court noted that "[a]dvance notice bylaws like the one at issue in this case are common," and that the board's decision to reject the Notice Letter as invalid was subject to the deferential business judgement rule.