Delaware Legislature Approves DGCL Amendments Endorsing Delaware Forum Selection Clauses and Prohibiting Fee-Shifting Provisions

As expected, the Delaware State Legislature approved amendments to the Delaware General Corporation Law (DGCL) that will (i) authorize forum selection clauses in the charters or bylaws of Delaware corporations specifying Delaware as an exclusive forum for litigating internal corporate claims, (ii) prohibit clauses designating only courts outside of Delaware as the exclusive forum for internal corporate claims and (iii) invalidate fee-shifting provisions in the charters or bylaws of Delaware stock corporations. The bill incorporating the amendments passed the Delaware Senate on May 12, 2015 and the Delaware House on June 11, 2015. If the Governor of Delaware signs the bill into law as expected, the amendments will become effective on August 1, 2015.

Forum Selection Clauses

Many Delaware corporations have adopted “internal affairs” forum selection clauses in their charters and bylaws in recent years in an attempt to limit duplicative litigation filed in multiple jurisdictions. Multiple forum litigation is expensive, distracting and frequently the result of jockeying among plaintiffs’ lawyers to obtain a “seat at the table” in lawsuits challenging mergers.

These forum selection clauses had never been the subject of legislation in Delaware; however, since 2013 the Delaware Court of Chancery has upheld several forum selection clauses. The new legislation will essentially codify the Delaware Court of Chancery’s June 2013 decision in Boilermakers Local 154 Retirement Fund v. Chevron Corporation, 73 A.3d 934 (Del. Ch. 2013), which upheld the statutory and contractual validity of board-adopted forum selection bylaws. Conversely, it will reject the Delaware Court of Chancery’s September 2014 decision in City of Providence v. First Citizens BancShares, Inc., 99 A.3d 229 (Del. Ch. 2014), which upheld the validity of a Delaware corporation’s board-adopted forum selection bylaw that designated North Carolina, the state in which the corporation is headquartered, as the exclusive forum for litigating internal corporate claims.

The amendments will add a new Section 115 to the DGCL authorizing the certificate of incorporation or bylaws of a Delaware corporation to include a forum selection clause requiring that lawsuits asserting “internal corporate claims,” including derivative actions, be brought solely and exclusively in the Delaware courts (including the federal court). Internal corporate claims are claims based on a violation of a duty by a current or former director or officer or stockholder in such capacity, and other claims as to which the DGCL confers jurisdiction upon the Delaware Court of Chancery.
New Section 115 will not expressly prohibit charter or bylaw provisions that select a forum other than the Delaware courts as an additional forum in which an internal corporate claim may be brought. However, the new Section 115 will invalidate any provision selecting only non-Delaware courts, or any arbitral forum, to the extent the provision would prohibit litigation of internal corporate claims in the Delaware courts. Thus, for example, it would be permissible for a Delaware corporation having its principal place of business or corporate headquarters in California to adopt a charter or bylaw provision designating both California and Delaware as the exclusive fora for bringing internal corporate claims, but it would be impermissible for the charter or bylaw provision to prescribe only California as the exclusive forum.

The amendments will not prohibit a clause selecting a forum other than Delaware as the exclusive forum if placed in a stockholders agreement or other writing signed by a stockholder against whom the forum selection clause is sought to be enforced. Furthermore, they will not shield from judicial review a claim that a forum selection clause operates unreasonably under the circumstances, or that the manner in which the clause was adopted was inequitable.

**Fee-Shifting Provisions**

Generally, in the United States (including Delaware), unless parties to a lawsuit have otherwise agreed by contract (or a specific statute provides that the court can allocate costs against a losing party), each litigant is responsible for paying its own attorneys' fees and court costs. Some jurisdictions outside the United States rely on a “loser pays” system to help discourage lawsuits of questionable merit and avoid pressures on corporations to settle non-meritorious suits early in order to avoid uncertainty and save the corporation time and money.

In May 2014, in *ATP Tour, Inc. v. Deutscher Tennis Bund*, 91 A.3d 554 (Del. 2014), the Delaware Supreme Court upheld the facial validity of a board-adopted bylaw of a Delaware nonstock corporation that provided for a losing plaintiff to pay the corporation’s attorneys’ fees and court costs associated with intracorporate litigation. Following the *ATP Tour* decision, which was not on its face limited to nonstock corporations, many Delaware stock corporations adopted or considered adopting “fee-shifting” bylaws. The amendments will limit the effect of the *ATP Tour* ruling by invalidating fee-shifting provisions in the charters and bylaws of Delaware stock corporations.

New DGCL Section 102(f) will provide that a certificate of incorporation may not contain any provision imposing liability on a stockholder for the attorneys’ fees or expenses of the corporation or any other party in connection with an “internal corporate claim” as defined in new Section 115. A similar proscription will be added to Section 109(b) of the DGCL, which addresses what provisions may be included in the bylaws of a Delaware corporation. Consistent with the *ATP Tour* decision, Section 114(b)(2) of the DGCL will be amended to make clear that the prohibition against fee-shifting provisions does not apply to Delaware nonstock corporations.

The amendments will not prohibit a fee-shifting provision in a stockholders agreement or other writing signed by a stockholder against whom the provision is sought to be enforced, nor will they impact other types of business entities, such as limited partnerships or limited liability companies, that are governed by separate statutory provisions.

This approach was the end result of a year-long debate over whether fee-shifting provisions should be allowed in any form, and, if so, how to draft a statute that would draw bright-line distinctions that would deter meritless
litigation, yet not chill the bringing of all “internal corporate claim” actions that may have plausible merit. In the end, the task proved too difficult and led to the blanket prohibition for all Delaware stock corporations, whether publicly or privately held.

Practical Implications

- Delaware corporations that have not previously adopted a Delaware forum selection clause should seriously consider adopting one. In doing so, companies should evaluate the voting policies of proxy advisory firms and institutional investors on forum selection clauses. Delaware corporations that have unilaterally adopted forum selection clauses in recent years generally have not faced significant adverse reaction from ISS or large institutional investors. However, under its current policies, Glass Lewis will consider recommending against the governance committee chair where the board adopted a forum selection bylaw in the past year without stockholder approval (and explicitly will recommend voting against the governance committee chair at companies that completed an IPO within the past year if the board unilaterally adopted a forum selection clause in the charter or bylaws prior to the IPO).

- If a Delaware corporation has adopted a forum selection clause that would prohibit litigation of internal corporate claims in the Delaware courts, it should amend the clause to make clear that such claims may be brought in Delaware in addition to, or instead of, the forum currently specified.

- A Delaware stock corporation that has adopted a fee-shifting provision should consider amending its charter and/or bylaws, as applicable, to remove such provision because it will no longer be enforceable once the new legislation takes effect.

If you have any questions regarding this Sidley Update, please contact the Sidley lawyer with whom you usually work, or

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