

Delaware Bar Proposes Amendments to Ban Fee-Shifting Provisions and Allow Delaware-Only Forum Selection Provisions in Corporate Charters and Bylaws

March 26, 2015 | Blog | By Chip Phinney

VIEWPOINT TOPICS

RELATED PRACTICES

RELATED INDUSTRIES

The Council of the Corporation Law Section of the Delaware State Bar Association recently released [proposed amendments to the Delaware General Corporation Law](#) (DGCL) that would prohibit fee-shifting provisions in a corporation's charter or bylaws for litigation involving the corporation's internal affairs, but authorize Delaware forum selection provisions. The proposal to ban fee-shifting provisions is particularly controversial and has generated significant debate over whether it is necessary to protect shareholder litigation or improperly deprives corporations of a needed tool to deter meritless suits. But the forum selection amendment also contains a thought-provoking element; while it permits Delaware corporations to designate courts in Delaware as the exclusive forum for certain types of corporate litigation, it would effectively prohibit them from selecting some other jurisdiction as the exclusive forum for that litigation.

Amendment to Ban Fee-Shifting Provisions

As we have [discussed previously](#), the Delaware Supreme Court held in *ATP Tour, Inc. v. Deutscher Tennis Bund*, 91 A.3d 554 (Del. 2014), that there is nothing in the Delaware General Corporation Law that would bar a corporation from adopting a bylaw holding an unsuccessful plaintiff liable for the defendant's attorneys' fees and costs in cases brought by a member against the corporation or another member, or by the corporation against a member. While the decision specifically concerned a non-stock corporation, the court's reasoning appeared to be equally applicable to a stock corporation. It has been reported that approximately [30 Delaware corporations have adopted fee-shifting bylaws](#) since the ATP decision. Plaintiffs' counsel have raised concerns that where a corporation has adopted a fee-shifting provision, the risk of incurring fees in an unsuccessful action will stifle shareholder suits.

In response to these concerns, the Council has proposed amending Sections 102 and 109 of the DGCL to add provisions stating that the certificate of incorporation and the bylaws of a Delaware corporation "may not contain any provision that would impose liability on a stockholder for the attorneys' fees or expenses of the corporation or any other party in connection with an intracorporate claim." "Intracorporate claims" are defined as "claims, including claims in the right of the corporation, (i) that are based upon a violation of a duty by a current or former director or officer or stockholder in such capacity, or (ii) as to which this title confers jurisdiction upon the Court of Chancery."

In an [accompanying explanation](#), the Council argues that proliferation of fee-shifting provisions would make even meritorious stockholder litigation "untenable." Since "[e]very lawsuit is a risk" in which the outcome cannot be confidently predicted, and "virtually no lawsuits of any type substantially achieve in substance and amount the full remedy sought," "few stockholders will rationally be able to accept the risk of exposure to millions of dollars in attorneys' fees to attempt to rectify a perceived corporate wrong, no matter how egregious." A resulting decline in stockholder litigation would curtail the development of the common law of corporations and undermine the enforcement of fiduciary duties. In the Council's opinion, judicial tools such as motions to dismiss, Rule 11 motions, court-ordered fee shifting, and the power to determine plaintiffs' attorneys' fee awards are better suited to control and deter unmeritorious litigation.

Not everyone agrees, of course. Lisa Rickard, President of the Institute for Legal Reform of the U.S. Chamber of Commerce, has been quoted as saying that the Council's proposed fee-shifting ban is "a huge win for Delaware's lawsuit business at the expense of shareholders in Delaware companies." A prominent member of the Delaware Bar has criticized the proposed amendment for ["using the dullness](#)

of a butter knife instead of the precision of a scalpel.” Professor Stephen Bainbridge of UCLA has opined that the Council’s proposal involves “a **serious policy error**” and questioned whether it is also “a serious tactical error” that could undermine Delaware’s primacy as a state of incorporation. Some of these critics have expressed particular concern about the epidemic of shareholder litigation over mergers and acquisitions, discussed [here](#) by our colleague Jonathan Shapiro. According to one study, in 2014 93 percent of M&A deals valued at over \$100 million were litigated. Proponents of fee-shifting bylaws believe that such loser-pays provisions offer an effective tool to deter such litigation when it is meritless.

Given the powerful forces on both sides of the debate, the ultimate outcome of the Council’s proposed amendment to ban fee-shifting provisions is difficult to predict and the development of the legislation will merit close monitoring for interested parties.

Amendment to Permit Delaware Forum Selection Provisions

The Council’s proposed amendments would also add a new section 115 to the DGCL stating that a corporation’s certificate of incorporation or bylaws “may require, consistent with applicable jurisdictional requirements, that any or all intracorporate claims shall be brought solely and exclusively in any or all of the courts in this State, and no provision of the certificate of incorporation or bylaws may prohibit bringing such claims in the courts of this State.” As stated in the synopsis at the end of the [proposed amendment](#), this provision codifies the holding of the Delaware Court of Chancery in [Boilermakers Local 154 Retirement Fund v. Chevron Corporation](#), 73 A.2d 934 (Del. Ch. 2013), permitting a Delaware corporation to adopt courts in Delaware as the exclusive forum for certain types of corporate litigation. The synopsis also make it clear that the phrase “the courts in this State” is intended to include the federal courts sitting in Delaware.

But the second part of the amendment goes further than *Boilermakers* insofar as it also prohibits a Delaware corporation from adopting a forum selection provision that would preclude litigation of intracorporate claims in the Delaware courts. Thus while the amendment permits Delaware corporations to adopt the courts in Delaware as the exclusive forum for intracorporate litigation, it bars Delaware corporations from specifying some other forum outside of Delaware as the exclusive forum for such litigation. This part of the amendment would effectively override the Court of Chancery’s decision last fall in [City of Providence v. First Citizens BancShares, Inc.](#), 99 A.3d 229 (Del. Ch. 2014), which upheld a bylaw specifying the U.S. District Court for the Eastern District of North Carolina or, if not available, the North Carolina state courts, as the exclusive forums for certain types of corporate litigation involving a Delaware corporation based in North Carolina, as discussed [here](#). Although there is an understandable rationale for requiring that the Delaware courts be available to litigants in cases involving the application of Delaware corporate law to Delaware corporations, one commentator has observed that the limitation of exclusive forum selection to Delaware alone gives “[the appearance of a litigation land grab](#).”

Authors



Chip Phinney