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CORPORATE GOVERNANCE

Viva Delaware!: Strine Upholds Board-Adopted Forum Selection Bylaws



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On June 25, 2013, the Delaware Court of Chancery handed down a much-anticipated opinion in *Boilermakers Local 154 Ret. Fund v. Chevron Corp.*, C.A. No. 7220-CS, 2013 BL 167755 (Del. Ch. June 25, 2013), upholding the statutory and contractual validity of forum selection bylaws that are adopted by boards of directors without shareholder approval. Because many companies incorporated in Delaware have their principal place of business elsewhere and have stockholders and operations in a myriad of states, often times companies are faced with similar, parallel litigation in several jurisdictions. This has been a particular nuisance in the wake of suits challenging mergers and acquisitions. Chancellor Leo E. Strine Jr.'s decision in *Chevron* will likely result in an influx of passage of similar bylaw provisions, which should have significant implications

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for corporate governance, particularly as a possible tool to combat costly multi-forum stockholder litigation.

The Rise of Forum Selection Clauses

The outcome of a case can vary considerably, depending on where it is filed. Almost any big merger or acquisition spurs a rush of multiple, duplicative lawsuits in various forums, as the plaintiffs' lawyers jockey for the most favorable jurisdictional position in the hopes of forcing a settlement. These parallel lawsuits cause companies to rack up significant legal fees and can subject corporations to inconsistent rulings in different jurisdictions.

More companies are incorporated in Delaware than any other state, largely because of its perceived company-friendly courts with well-developed precedent for corporate issues. Indeed, contracts routinely include forum selection clauses requiring that lawsuits arising under or relating to them be brought in a particular jurisdiction, often Delaware. In his 2010 decision in *In re Revlon, Inc. S'holders Litig.*, 990 A.2d 940 (Del. Ch. 2010), Vice Chancellor Laster suggested that corporations concerned about the perils of multi-forum litigation could take forum selection a step further and amend their charters to pre-designate their preferred judicial arena, as well. In the wake of this perceived signal from the Delaware Chancery Court, as many as 250 public companies adopted bylaws or amended their charters with forum selection clauses designating Delaware as the exclusive forum for shareholder suits.

Challenges to Board-Adopted Provisions Lacking Shareholder Approval

The first challenge to this forum selection bylaw phenomenon resulted in a win for the plaintiffs' firms. In January 2011, the U.S. District Court for the Northern District of California refused to enforce a forum selection bylaw that had been adopted by Oracle Corporation because it had not been adopted by the company's stockholders, but instead had been unilaterally-adopted by the board of directors. In *Galaviz v. Berg*, 763

F. Supp. 2d 1170 (N.D. Cal. 2011), the court noted the overwhelming precedent for upholding contractual forum selection clauses, but differentiated a forum selection clause in a bargained-for contract from a similar provision in unilaterally-adopted bylaws. Although Oracle argued that a bylaw should be treated as any other contract, the Northern District of California declined to so hold, particularly in light of the bylaw provisions' unilateral nature. The court went a step further, questioning whether the Delaware General Corporate Law ("DGCL") allowed unilateral board adoption of a forum selection bylaw.

This spawned a flurry of lawsuits in Delaware Chancery Court against twelve companies whose boards of directors had also unilaterally adopted forum selection bylaws without shareholder approval, including Chevron Corporation and FedEx Corporation. Ten of the twelve companies repealed their bylaws immediately. However, Chevron and FedEx, both incorporated in Delaware with principle places of business elsewhere, stuck to their guns, and the two cases were consolidated.

Details of Chevron's and FedEx's Challenged Bylaws

The boards of directors of Chevron and FedEx, without seeking shareholder approval, adopted forum selection bylaws designating Delaware as the exclusive forum for: (1) derivative suits; (2) actions for breaches of fiduciary duty; (3) actions asserting claims under the DGCL; and (4) actions relating to the "internal affairs" of the corporation.

The plaintiffs challenged the forum selection bylaws and the boards' actions, contending that the bylaws: (1) were statutorily invalid and improper under the DGCL; (2) were invalid as a matter of contract law; and (3) that the Chevron and FedEx boards breached their fiduciary duties in adopting the provisions.

Chancellor Strine's June 25 opinion granted the defendants' motion for judgment on the pleadings, rejecting the plaintiffs' first two arguments (and declining to reach the third).

Chancellor Strine Upholds Forum Selection Bylaws as Facially Valid

First, with respect to the plaintiffs' statutory claim, Chancellor Strine ruled (in stark contrast to the *Galaviz* court) that unilaterally-adopted forum selection bylaw provisions were plainly authorized under the DGCL. Section 109(b) of the DGCL provides that corporate bylaws may contain any provision relating to "the business of the company, the conduct of its affairs, and its right or powers or the right or powers of its stockholders, directors, officers and employees." Chancellor Strine rebuffed the plaintiffs' assertions that the provisions at issue did not relate to any of the enumerated purposes in the DGCL. The court found it obvious that forum selection bylaws clearly govern disputes related to the internal affairs of the corporations, and also relate to stockholders' rights by designating the forum in which stockholders can bring certain claims. The court compared its holding to the Delaware Supreme Court's decision upholding poison pill rights plans in *Moran v.*

Household Int'l, Inc., 500 A.2d 1346 (Del. 1985), explaining that

[j]ust as the board of Household was permitted to adopt the pill to address a future tender offer that might threaten the corporation's best interests, so too do the boards of Chevron and FedEx have the statutory authority to adopt a bylaw to protect against what they claim is a threat to their corporations and stockholders, the potential for duplicative law suits in multiple jurisdictions over single events.

Following the *Galaviz* plaintiffs' lead, the plaintiffs also claimed that the bylaws were invalid as a matter of contract law because they were adopted unilaterally by the boards of directors of Chevron and FedEx without stockholder consent.

While this argument carried the day with the Northern District of California, Chancellor Strine didn't buy it, criticizing the *Galaviz* court's "failure to appreciate the contractual framework established by the DGCL."

The court explained that the DGCL allows the corporation, through the certificate of incorporation, to grant the directors the power to adopt and amend the bylaws unilaterally. Because the certificates of incorporation of Chevron and FedEx contained provisions conferring such powers upon their boards, when the plaintiffs purchased stock in these corporations, they were on notice of the boards' powers to unilaterally adopt bylaw provisions without notice to, or approval by, the stockholders.

Chancellor Strine drew no distinction between bylaws, which he characterized as flexible and binding contracts between a company and its stockholders, and any other contract: "A forum selection clause adopted by a board with the authority to adopt bylaws is valid and enforceable under Delaware law to the same extent as other contractual forum selection clauses." And in any event, Chancellor Strine noted that forum selection clauses are presumed valid in Delaware.

Finally, the court declined to entertain the plaintiffs' list of hypothetical situations in which forum selection bylaws might be unreasonable, reminding the plaintiffs that the Delaware Chancery Court does not render advisory opinions on "conjured-up" "parade[s] of horrors."

Chancellor Strine acknowledged that there exist clear limits on a board's right to unilaterally adopt forum selection bylaws. First, in order to fall under the statutory authorization of the DGCL, forum selection bylaws must relate to suits brought by stockholders in cases governed by the internal affairs doctrine. Under the DGCL, stockholders' power to amend or repeal any bylaws "is legally sacrosanct." Moreover, these bylaw provisions will be subject to the same scrutiny as other contractual forum selection clauses under the United States Supreme Court's decision in *M/S Bremen v. Zapata Off-Shore Co.*, 407 U.S. 1 (1972), holding that forum selection clauses that are unreasonable or unjust will not be upheld.

Impact

While the plaintiffs will almost certainly appeal this decision, it still provides corporations with strong support to adopt a forum selection bylaw to attempt to combat the number of parallel lawsuits brought against the company in the wake of a large deal. This will also increase the predictability of outcomes of cases brought against a corporation, as more and more suits are nec-

essarily brought in that company's designated jurisdiction.

It is important to remember, however, that Chancellor Strine's opinion only upholds bylaw provisions relating to the internal affairs of the company under the DGCL. Accordingly, corporations will not necessarily be able to pre-designate a preferred jurisdiction for a variety of other litigation through this avenue. Of

course, a stockholder could also take a chance and file suit for an internal affairs issue outside of the company's bylaw-designated jurisdiction, in which case it remains to be seen whether other courts will follow the Delaware Chancery Court's precedent and relinquish their previously-held jurisdiction over cases that may now be subject to a forum selection bylaw.