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Forum Selection Bylaws Help Combat Multijurisdictional Shareholder Litigation: State Courts are Increasingly Upholding Forum Selection Provisions in Corporate Bylaws

Robert A. Friedel | friedelr@pepperlaw.com, Melissa L. Nuñez | nunezm@pepperlaw.com

When almost 98 percent of takeover transactions valued at more than $100 million result in shareholder litigation,[1] and often such transactions are the subject of multiple lawsuits filed in multiple jurisdictions, it is no surprise that companies are looking for ways to make such litigation more manageable and efficient. In 2010, Delaware Court of Chancery Vice Chancellor J. Travis Laster proposed one such method, writing in an opinion that "corporations are free to respond with charter provisions selecting an exclusive forum for intra-entity disputes"[2] if boards believe this would benefit the corporation. Thus began a rapid upswing in the number of adoptions of forum selection bylaws by public companies.

After an early move by a California court in opposition to the enforceability of forum selection bylaws in a 2011 decision, the recent case of *Groen v. Safeway*[3] represents a clear move by California to join the growing list of states going on record to endorse the enforceability of such clauses.

What Is a Bylaw Forum Selection Provision?

In general, a forum selection provision in a corporation's charter or bylaws names a particular state – typically the state of incorporation – that will be the sole and exclusive forum for derivative lawsuits, breach of fiduciary duty lawsuits, claims arising under the state's corporate law, and claims relating to the internal affairs of the company. Forum selection provisions are typically contained in a corporation's bylaws given that, in contrast to charter amendments, which typically require stockholder approval, bylaws may routinely be amended by action of the board of directors alone. Given the substantial percentage of U.S. public companies that are incorporated in Delaware, most of the litigation thus far concerning the enforceability of forum selection bylaw provisions has involved bylaw provisions selecting Delaware as the exclusive jurisdiction.

Why Adopt a Bylaw Forum Selection Provision?

The principal benefit of adopting a forum selection provision is to minimize the risk of multi-jurisdictional litigation, which can otherwise force a company to litigate the same claims at the same time in two or more different jurisdictions. An added benefit for Delaware corporations is that the Delaware Court of Chancery is generally more experienced at dealing with intra-corporate disputes in comparison to a court of another state that may be unfamiliar with these types of disputes and even less familiar with the applicable Delaware law underlying the claim.

Delaware's Position

In 2013, the Delaware Court of Chancery upheld forum selection bylaw provisions in *Boilermakers Local 154 Retirement Fund v. Chevron Corporation*,[4] holding that forum selection bylaw provisions are valid under Delaware law. And if the bylaws authorize amendments by the board of directors without shareholder approval, a forum selection provision adopted by board action alone is enforceable against shareholders, including those who own shares at the time of the adoption.

The court noted that although a forum selection provision would be presumptively valid, a plaintiff burdened by such a provision could still challenge the application of such a provision on a case-by-case basis for breach of fiduciary duty or under general rules of contract law as set forth by the U.S. Supreme Court in *The Bremen v. Zapata Off-Shore Company*.[5] Delaware case law follows the general rule set forth by *Bremen*

that a forum selection provision should be specifically enforced unless the party seeking to invalidate the clause could clearly show that enforcement would be unreasonable and unjust, or that the forum selection clause was invalid due to fraud or overreaching. Nevertheless, this potential risk of unenforceability in specific applications has not slowed the wave of adoptions of forum selection provisions by companies that has followed the *Boilermakers* decision.

California Case Law

In 2011 (two years before the *Boilermakers* decision), the U.S. District Court for the Northern District of California refused to enforce a forum selection provision in *Galaviz v. Berg*.[6] In *Galaviz*, the forum selection provision in question was adopted by the board, without shareholder approval, after a majority of the alleged wrongdoing at issue in the underlying litigation had already occurred. As a result, the court declined to enforce the provision.

Three years later, in May 2014, in *Groen v. Safeway, Inc.*,[7] a California court followed Delaware's lead in *Boilermakers* and upheld the enforceability of Safeway's forum selection provision adopted by the board without shareholder approval and, as a result, dismissed shareholder derivative actions filed in California arising from Safeway's merger announcement. In its decision, the court noted that *Galaviz* was decided before *Boilermakers*, implying that *Galaviz* was no longer good law. Ultimately, the court determined that the provision withstood a facial challenge and that, because there was not support for the plaintiffs' claim that the provision was adopted after wrongdoing had occurred, it also withstood an as-applied challenge.

Conclusion

Acceptance of forum selection provisions in bylaws is growing, as illustrated by *Groen*. *Groen's* implication that *Galaviz* is no longer good law adds further momentum to the legal strength of such provisions. Because the law of bylaw forum selection provisions is relatively new and is still evolving, courts in many states have not yet weighed in on their enforceability, and a state court in Oregon has recently signaled a move counter to the trend of enforceability of such provisions.[8] Nevertheless, *Groen* adds California to the growing list of states that have upheld such provisions, following Delaware, New York,[9] Illinois,[10] Louisiana[11] and Texas.[12]

Boards of directors of public companies should now consider adopting bylaw forum selection provisions in order to guard against having to defend future fiduciary duty or other internal affairs litigation matters simultaneously in multiple jurisdictions.

> ***Pepper Point:*** *Because forum selection provisions are not effective to deny the ability of stockholders to seek the judicial resolution of disputes, it is advisable for the board of directors to consider the adoption of such provisions at a time when the company is not anticipating any litigation that would be subject to such a provision. Before amending bylaws to include a forum selection provision, companies should thoroughly review all relevant corporate governance documents to ensure compliance with applicable approval processes and should consult counsel with respect to the method and necessity of disclosing any such adoption.*

For further reading, please see the Client Alert below previously published by Pepper Hamilton:

Delaware Non-Stock Corporations May Adopt Bylaws that Shift Fees to Unsuccessful Plaintiffs in Intra-Corporate Litigation (http://www.pepperlaw.com/publications_update.aspx?ArticleKey=2939).

Endnotes

1 Matthew D. Cain and Steven M. Davidoff, Takeover Litigation in 2013 (January 9, 2014).

2 *In re Revlon, Inc. Shareholders Litigation*, 990 A.2d 940 (Del. Ch. 2010).

3 No. RG14716641 (Super. Ct. of Cal., Alameda County, May 14, 2014).

4 73 A.3d 934 (Del. Ch. 2013).

5 407 U.S. 1 (1972).

6 763 F.Supp.2d 1170 (N.D. Cal. 2011).

7 No. RG14716641 (Super. Ct. of Cal., Alameda County, May

14, 2014).

8 *See Roberts v. TriQuint Semiconductor, Inc.*, No. 1402-02441 (Cir. Ct. Or., Aug 14, 2014), in which the court held that a bylaw forum selection provision was unenforceable where the provision was adopted by the board, without shareholder approval, after the board's alleged wrongdoing, in a fact pattern similar to that in Galaviz.

9 *See Hemg Inc. v. Aspen University*, No. 650457/13, 2013 WL 5958388 (N.Y. Sup. Ct., Nov. 4, 2013).

10 *See Miller v. Beam Inc.*, No. 2014 CH 00932 (March 5, 2014).

11 *See Genoud v. Edgen Group Inc., et al.*, Case No. 625,244 (19th Dist. Ct., Parish of E. Baton Rouge).

12 *See In re MetroPCS Commc'ns, Inc.*, 391 S.W.3d 329 (Tex. App. 2013).