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DELAWARE CHANCERY COURT UPHOLDS VALIDITY OF "FORUM SELECTION BYLAWS"

Faced with burdensome and duplicative multi-forum litigation, the boards of many corporations have recently adopted bylaws requiring that lawsuits relating to the corporation's internal affairs be brought only in designated courts. Lifting the "cloud" cast by shareholder lawsuits challenging these "forum selection bylaws," Chancellor Leo E. Strine of the Delaware Chancery Court issued a decision on June 25, 2013 holding that forum selection bylaws are facially and presumptively valid under Delaware law and that the Delaware Court of Chancery will enforce these bylaws in the same way it enforces contractual forum selection clauses.

In *Boilermakers Local 154 Retirement Fund et al. v. Chevron Corporation et al.* (Civil Action No. 7220) and *IClub Investment Partnership et al. v. FedEx Corporation et al.* (Civil Action No. 7238), which were consolidated for purposes of the decision, shareholders sued the boards of Chevron and FedEx respectively for adopting bylaws requiring that certain lawsuits be brought in Delaware courts. The forum selection bylaws adopted by Chevron and FedEx, both of which are incorporated in Delaware, specifically applied to (i) lawsuits brought on behalf of the corporation (derivative suits), (ii) claims of breach of fiduciary duty owed by directors, officers or employees to the corporation or its stockholders, (iii) claims brought pursuant to the Delaware General Corporation Law ("DGCL"), and (iv) any action asserting a claim governed by the "internal affairs" doctrine, meaning matters peculiar to the relationships among or between the corporation and its officers, directors, and shareholders. Plaintiffs asserted that the forum selection bylaws were statutorily invalid because they go beyond the board's authority under the DGCL and that they are contractually invalid because they were unilaterally adopted as bylaws by the Chevron and FedEx boards.

Chancellor Strine found that the forum selection bylaws did not exceed the board's authority under the DGCL, since they regulate only the forum of suits brought by stockholders *qua* stockholders in cases governed by the internal affairs doctrine. Chancellor Strine also found that forum selection bylaws are valid and enforceable contractual forum selection clauses when the certificate of incorporation gives the board the power to adopt and amend the bylaws unilaterally, as is permitted under the DGCL. When they buy stock, stockholders contractually assent to the board's authority to adopt binding bylaws, including forum selection bylaws, regulating the corporation's internal affairs. The Court noted, however, that shareholders are protected by several safeguards, chief among them that under Delaware law shareholders may repeal by majority vote any bylaws unilaterally adopted by the board of directors.

The Court was careful to limit its ruling to the *facial* validity of forum selection bylaws, purposefully leaving open challenges to the "real-world" enforcement of such bylaws. Chancellor Strine explained that under *Schnell v. Chris-Craft Industries, Inc.*, 285 A.2d 437, 439 (Del. 1971) plaintiffs may challenge any bylaws, including forum selection bylaws, as being used for "inequitable purposes" in breach of fiduciary duties. Chancellor Strine also held that, since forum selection bylaws will be construed like any other contractual forum selection clause, they will be subject to scrutiny under the principles of The *Bremen v. Zapata Off-Shore Co.*, 407 U.S. 1 (1972), as adopted by the Delaware Supreme Court in *Ingres Corp. v. CA, Inc.*, 8 A.3d 1143, 1146 (Del. 2010). That is, forum selection clauses (and bylaws) are valid provided they are "unaffected by fraud, undue influence, or overweening bargaining power," and "should be enforced unless enforcement is shown by the resisting party to be 'unreasonable.'" Ultimately, courts following Delaware law will assess the reasonableness of applying forum selection bylaws on a case-by-case basis.

Chancellor Strine noted that his decision is in part intended to give broad-based guidance to foreign courts, which, if they respect the internal affairs doctrine, should apply the law of the state of incorporation to determine the enforceability of bylaws. Such guidance was necessary because, for example, a federal district court in the Northern District of California held in 2011 that a forum selection bylaw was unenforceable because it was adopted without the consent of existing shareholders. *See Galaviz v. Berg*, 763 F. Supp. 2d 1170 (N.D. Cal. 2011). That opinion was issued without the benefit of Delaware (or any) case-law directly addressing the validity of such bylaws. Moreover, the directors in that case adopted the bylaws after they committed the alleged wrongdoing.

Chancellor Strine's decision makes clear that, under Delaware law, forum selection bylaws are not invalid on their face. Rather, they are presumptively valid and will be treated like any other forum selection clause. As such, boards of directors that are empowered to adopt bylaws should seriously consider adopting forum selection bylaws to avoid duplicative suits and thus to help manage litigation costs.

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If you have any questions or need additional information about this Alert, please contact the following attorneys:

Arthur H. Aufses, III
Partner
aaufses@kramerlevin.com
212.715.9234

Abbe L. Dienstag
Partner
adienstag@kramerlevin.com
212.715.9280

Alan R. Friedman
Partner
afriedman@kramerlevin.com
212.715.9300

Kenneth P. Kopelman
Partner
kkopelman@kramerlevin.com
212.715.9358

Jonathan M. Wagner
Partner
jwagner@kramerlevin.com
212.715.9393

Tobias B. Jacoby
Associate
tjacoby@kramerlevin.com
212.715.9332

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