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DELAWARE LAW

# Fee-Shifting Bylaws: Where Are We Now?

BY CLAUDIA H. ALLEN

Since the Delaware Supreme Court unexpectedly upheld the facial validity of fee-shifting bylaws for non-stock corporations in *ATP Tour, Inc. v. Deutscher Tennis Bund*,[1] opponents have employed heated rhetoric suggesting that such bylaws could eliminate stockholders' ability to seek redress for wrongdoing.[2] The decision swiftly prompted draft legislation that would have amended the Delaware General Corporation Law to broadly prohibit fee-shifting and other provisions in bylaws and certificates of incorporation imposing liability on stockholders.[3] Shortly before anticipated passage, and following criticism from the U.S. Chamber of Commerce and some public companies,[4] the legislation was tabled, subject to being

*Claudia H. Allen is a partner and co-chair of the Corporate Governance practice at Katten Muchin Rosenman LLP. She counsels boards, management and investors in public and private companies on corporate governance matters and related issues, such as shareholder activism and engagement, fiduciary duties and board/committee process and structure. Her practice also encompasses transactional matters, including private and public mergers and acquisitions, and securities law matters.*

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[1] 91 A.3d 554 (Del. May 8, 2014). The opinion, which responded to certified questions of law from the U.S. District Court for the District of Delaware, did not address whether the ATP bylaw is enforceable.

In addition, the Court did not state whether the opinion would also apply to traditional, rather than non-stock, corporations. Note, however, that Del. Code tit. 8, § 114 (Application of Chapter to Nonstock Corporations) states that most provisions of the Delaware General Corporation Law, including § 109(b) (Bylaws) concerning the permissible scope of bylaws, apply to non-stock corporations, and all references to stockholders are deemed to apply to the members of a non-stock corporation. *See ATP* at 557 n.10.

[2] *See, e.g.*, Letter from the American Federation of Labor and Congress of Industrial Organizations, seven other labor unions and the National Conference on Public Employee Retirement Systems to The Hon. Jack Markell, Governor of Delaware (Dec. 3, 2014) (''We write to express our serious concerns regarding the national and sweeping implications of a recent Delaware Supreme Court decision which eviscerates investors' rights and threatens the security of US capital markets.''). In addition, some have called for the Securities and Exchange Commission to examine fee-shifting. *See, e.g.*, John C. Coffee, Jr., *''Loser Pays'': Who Will Be the Biggest Loser?*, CLS Blue Sky Blog (Nov. 24, 2014), http://clsbluesky.law.columbia.edu/2014/11/24/loser-pays-who-will-be-the-biggest-loser/.

[3] Delaware State Senate, 147th General Assembly, SB 236 (An Act to Amend Title 8 of the Delaware Code Relating to General Corporation Law), http://www.legis.delaware.gov/LIS/LIS147.NSF/vwLegislation/SB+236?Opendocument. That legislation was generally supported by both the defense and plaintiffs' bar in Delaware.

For purposes of this Article, the terms ''certificate of incorporation'' and ''charter'' are used interchangeably.

[4] *See, e.g.*, Jonathan Starkey, *Delaware Lawyers Fight Fee-Shifting in Legislature*, NEWS J. (June 10, 2014), http://www.delawareonline.com/story/news/local/2014/06/09/

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revisited during the 2015 legislative session.[5] Also signaling controversy, stockholders have mounted at least three challenges to fee-shifting bylaws, of which two were voluntarily withdrawn,[6] and a third, involving a formerly public company, is pending in the Delaware Court of Chancery.[7]

In view of the attention being focused upon these provisions, this article seeks to analyze the limited universe of provisions adopted since *ATP*.

## The ATP Template

The bylaw adopted by ATP Tour has become the de facto template for most of the provisions adopted to date. The bylaw, which was adopted in 2006, provides in pertinent part:

> (a) In the event that (i) any [current or prior member or Owner or anyone on their behalf (''Claiming Party'')] initiates or asserts any [claim or counterclaim (''Claim'')] or joins, offers substantial assistance to or has a direct financial interest in any Claim against the League or any member or Owner (including any Claim purportedly filed on behalf of the League or any member), and (ii) the Claiming Party (or the third party that received substantial assistance from the Claiming Party or in whose Claim the Claiming Party had a direct financial interest) does not obtain a judgment on the merits that substantially achieves, in substance and amount, the full remedy sought, then each Claiming Party shall be obligated jointly and severally to reimburse the League and any such member or Owners for all fees, costs and expenses of every kind and description (including, but not limited to, all reasonable attorneys' fees and other litigation expenses) (collectively, ''Litigation Costs'') that the parties may incur in connection with such Claim.[8]

As is apparent from the text, this provision is not a bilateral ''loser pays'' provision. Rather, fees are only shifted to the plaintiff and specified related parties. At the same time, such parties will automatically be responsible for the defendants' fees, costs and expenses unless they:

- reach a ''judgment on the merits,'' which may be difficult since most cases are resolved by settlement, and
- such judgment ''substantially achieves . . . the full remedy sought,'' in substance and amount, meaning that even if the plaintiff wins on some counts, it may still be liable for all of the defendants' fees, costs and expenses.

It is worth noting that a modest number of public companies adopted various forms of fee-shifting prior to *ATP*. For example, beginning in 2008, a group of related companies adopted fee-shifting bylaws or, in some cases, amendments to their declarations of trust,[9] as exemplified by the bylaw adopted by Hospitality Properties Trust:

> Section 15.2. Costs and Expenses. To the fullest extent permitted by law, each shareholder will be liable to the Trust for, and indemnify and hold harmless the Trust (and any subsidiaries or affiliates thereof) from and against, all costs, expenses, penalties, fines or other amounts, including without limitation, reasonable attorneys' and other professional fees, whether third party or internal, arising from such shareholder's breach of any provision of these Bylaws or the Declaration of Trust or any action against the Trust in which such shareholder is not the prevailing party, and shall pay such amounts on demand, together with interest on such amounts, which interest will accrue at the lesser of the Trust's highest marginal borrowing rate, per annum compounded, and the maximum amount permitted by law, from the date such costs or the like are incurred until the receipt of payment.[10]

Some of the clauses in this bylaw that are not in the ATP model, such as those creating liability for breach of the bylaws or declaration of trust and requiring payment of interest, have been included in certain recently adopted provisions, as discussed below.[11]

## How Many Provisions Were Adopted and by Whom?

Since *ATP*, and despite claims that large numbers of public companies would adopt fee-shifting bylaws, only 39 domestic corporations,[12] out of the approximately

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delaware-lawyers-push-bill-protect-legal-fees/10260555/; Letter from Lisa A. Rickard, President, U.S Chamber Institute for Legal Reform to Members of the Delaware General Assembly (June 9, 2014); Letter from C. Michael Carter, President and Chief Operating Officer of Dole Food Company, Inc. to The Hon. Bryan Townsend (June 9, 2014).

[5] Delaware State Senate, 147th General Assembly, Senate Joint Resolution No. 12 (Calling for Continued Examination of Important Proposed Amendments to the Delaware General Corporation Law Relating to Fee-Shifting and Other Aspects of Corporate Litigation).

[6] Pignatelli v. Biolase, Inc., C.A. No. 9920-VCN (Del. Ch. filed July 21, 2014) was dismissed without prejudice. In *Kastis v. Carter*, C.A. No. 8657-CB (Del. Ch. 2014), counsel to Hemispherx Biopharma, Inc. sent a letter to Chancellor Bouchard on Sept. 16, 2014 stating: ''I write to advise the Court and counsel . . . that Hemispherx Biopharma, Inc. and the individual defendants have elected not to apply Hemispherx's fee-shifting bylaw to any aspect of this action . . . We understand that as a result, plaintiffs' challenge to the validity of the bylaw will not be litigated in this action.''

[7] Strougo v. Hollander, C.A. No. 9770-CB (Del. Ch. amended complaint filed Sept. 24, 2014).

[8] *ATP* at 556.

[9] A declaration of trust is analogous to a certificate of incorporation.

[10] Hospitality Properties Trust, Amended and Restated Bylaws, dated Nov. 6, 2008. Filed as Exhibit 3.1 to Quarterly Report on Form 10-Q filed on Nov. 10, 2008, *available at* http://www.sec.gov/Archives/edgar/data/945394/000110465908069763/a08-25351_1ex3d1.htm. Like many of the related entities, Hospitality Properties Trust was formed in Maryland.

[11] Other companies that adopted fee-shifting provisions include several funds in the Invesco family of funds. *See, e.g.*, Section 8.5 of Exhibit E to the Definitive Proxy Statement on Schedule 14A filed on June 14, 2012, *available at* http://www.sec.gov/Archives/edgar/data/5094/000095012312009092/h86559ddef14a.htm.

[12] *See* chart on p. 7. This total includes First Aviation Services, Inc., which is no longer publicly traded, and excludes Alibaba Group Holding Limited, which is a Cayman Islands corporation. Alibaba went public during this period and included a fee-shifting provision in its Memorandum of Association (which is analogous to a certificate of incorporation). *See* Alibaba Group Holding Limited, Form of Amended and Restated Memorandum of Association to be effective upon closing of IPO. Filed as Exhibit 3.2 to Amendment No. 6 to Registration Statement on Form F-1A filed on Sept. 5, 2014, *available at* http://www.sec.gov/Archives/edgar/data/1577552/000119312514333674/d709111dex32.htm. While Alibaba's fee-shifting provision attracted significant attention, in part due to

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5,000 public companies traded on U.S. stock exchanges[13] have acted. In addition, while not the focus of this Article, 13 limited partnerships,[14] all of which were formed in Delaware and 76.9 percent (10) of which are in the energy sector, have included fee-shifting provisions in their limited partnership agreements as they go public (or, in one case, convert to a limited partnership).

Of the domestic corporations, 89.7 percent (35) adopted bylaws, while 10.3 percent (4) included provisions in their certificates of incorporation. The 33 corporations that were already public adopted bylaws through unilateral board action, with one corporation announcing that it will put its bylaw to a stockholder vote. Of the six IPO companies, four adopted charter provisions, while two adopted bylaws. Unlike bylaws, charter provisions may only be amended with the vote of both the board and stockholders. IPO companies tend to include controversial provisions in their charters, rather than their bylaws, since bylaws are subject to amendment by stockholders, who thus have the power to remove such provisions.

Based upon data from Yahoo Finance, the market capitalization of the 34 corporations for which data is available[15] breaks down as follows:

**Market Capitalization of Corporations With Fee-Shifting Provisions**

| Capitalization | Number | % |
|---|---|---|
| up to $10 million | 3 | 8.9% |
| $10 – $49 million | 6 | 17.6% |
| $50 – $99 million | 6 | 17.6% |
| $100 – $999 million | 8 | 23.5% |
| $1 – $4.5 billion | 11 | 32.4% |
| Total | 34 | 100% |

Source: Claudia Allen — A BNA Graphic/ leg012g1

Thus, no large cap companies have adopted fee-shifting, and 67.6 percent (23) of the 34 companies have market caps below (and in many cases significantly below) $1 billion.

In terms of state of incorporation, 76.9 percent (30) of the corporations analyzed were formed in Delaware, which is not surprising given that *ATP* was a Delaware decision and that Delaware is the most common state of incorporation for public companies. The remaining 23.1 percent (9) companies were incorporated in the following states: Maryland (1), Minnesota (1), Missouri (1), Nevada (3), Ohio (1), Utah (1) and Virginia (1), thus reflecting the influence of the Delaware courts in other states.

In terms of the rate of adoption, the data breaks down as follows[15]:

**Adoption of Fee-Shifting Provisions in 2014 by Month**

| Month | Number |
|---|---|
| May | 1 |
| June | 4 |
| July | 5 |
| Aug. | 1 |
| Sept. | 3 |
| Oct. | 6 |
| Nov. | 8 |
| Dec. | 8 |
| Total | 36 |

Source: Claudia Allen — A BNA Graphic/leg012g2

While there is a general upward trend, it is difficult to draw firm conclusions since the sample size is small and the time period is relatively short.

## What Were the Circumstances of Adoption?

Several of the fee-shifting provisions were not adopted in the ordinary course of business. For example,

- three companies adopted bylaws in connection with threatened or actual proxy contests,
- three adopted them during ongoing litigation,
- two adopted them in connection with signing or closing a transaction,
- one adopted a bylaw after certain subsidiaries filed for bankruptcy protection,
- one adopted a bylaw after announcing a government investigation, and
- one adopted a bylaw after announcing a reverse stock split.[17]

If the board adopts a fee-shifting bylaw on a ''cloudy day,'' plaintiffs may have additional bases for arguing that directors were trying to improperly insulate themselves from liability and that enforcement would be inequitable. As noted in *ATP*, ''[b]ylaws that may other-

its $25 billion IPO, Alibaba is subject to a different corporate law system and SEC rules that vary in many respects from those applicable to domestic issuers.

[13] Dan Strumpf, *U.S. Public Companies Rise Again*, WALL ST. J., Feb. 5, 2014. This statistic includes foreign companies trading on domestic exchanges.

[14] *See* chart on p. 7 for a list of the limited partnerships. Such master limited partnerships are not subject to the same fiduciary regime as corporations.

[15] The capitalizations were collected after SEC filings announcing adoption of a fee-shifting provision.

[15] Two additional companies whose IPO registration are not effective and one company that intends to adopt a fee-shifting bylaw in connection with its proposed corporate reorganization are not included in the total.

[17] Certain companies are included in more than one category.

wise be facially valid will not be enforced if adopted or used for an inequitable purpose.''[18]

## What Do the Provisions Look Like?

The fee-shifting bylaw adopted by Echo Therapeutics, Inc. on June 24, 2014 is representative and largely reflects the ATP model:

> 5.13 Litigation Costs. To the fullest extent permitted by law, in the event that (i) any current or prior stockholder or anyone on their behalf (''Claiming Party'') initiates or asserts any claim or counterclaim (''Claim'') or joins, offers substantial assistance to, or has a direct financial interest in any Claim against the Corporation and/or any Director, Officer, Employee or Affiliate, and (ii) the Claiming Party (or the third party that received substantial assistance from the Claiming Party or in whose Claim the Claiming Party had a direct financial interest) does not obtain a judgment on the merits that substantially achieves, in substance and amount, the full remedy sought, then each Claiming Party shall be obligated jointly and severally to reimburse the Corporation and any such Director, Officer, Employee or Affiliate, the greatest amount permitted by law of all fees, costs and expenses of every kind and description (including but not limited to, all reasonable attorney's fees and other litigation expenses) (collectively, ''Litigation Costs'') that the parties may incur in connection with such Claim.[19]

The language in this and other fee-shifting provisions is broadly drawn, raising questions as to how the bylaws would operate in practice. For example, it is not clear what providing ''substantial assistance'' means. Some lawyers representing plaintiffs in lawsuits challenging fee-shifting bylaws have argued that the language would reach them personally, thus making it economically unfeasible for them to represent the plaintiffs.[20] At the same time, as discussed below, companies have experimented with a variety of clauses.

### High Standard for Plaintiffs

Consistent with the ATP bylaw, 82.1 percent (32) of the analyzed provisions require that the plaintiff achieve a judgment on the merits that ''substantially achieves'' the full remedy sought in order to avoid the obligation to reimburse the company. Alternatives to this formulation require that:

- the plaintiff be the prevailing party (10.3 percent, 4 companies),
- the plaintiff achieve a judgment on the merits in its favor (2.6 percent, 1 company), or
- the court make a determination that the proceeding ''resulted in a substantial benefit'' to the company (2.6 percent, 1 company).[21]

As a practical matter, it is not clear whether the first two alternatives require a complete victory. The third formulation employs language that is well known to the courts.

### Additional Trigger for Liability; Indemnification; Interest

Three companies adopted bylaws that largely reflect pre-ATP provisions.[22] In each case, stockholders are required to indemnify the company and its subsidiaries and affiliates for any amounts ''arising from such stockholder's breach of or failure to fully comply with any covenant, condition or provision of these by-laws or the certificate of incorporation,''[23] including those relating to fee-shifting, exclusive forum (discussed *below*) and other litigation matters. These non-specific provisions are broadly drawn and could arguably cover matters such as nominating a director candidate or proposing a matter to be brought before a stockholders meeting, but not complying with the associated disclosure obligations, which may be extensive. The language could thus make it very expensive to challenge the scope of an advance notice bylaw.

The indemnification obligation covers breach/noncompliance as well as fee-shifting obligations. Furthermore, each of the three companies requires that the stockholder pay interest on the amount to be indemnified at a rate equal to ''the lesser of the corporation's highest marginal borrowing rate and the maximum amount permitted by law, from the date such costs or the like are incurred until the receipt of payment.'' The

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[18] *ATP* at 558. The court cited to *Schnell v. Chris-Craft Industries*, 285 A.2d 437, 439 (Del. 1971) for the premise that ''inequitable action does not become permissible simply because it is legally possible.'' At the same time, the court in *ATP* stated that ''[t]he intent to deter litigation . . . is not invariably an improper purpose.'' *ATP* at 560.

[19] Echo Therapeutics, Inc., Amended and Restated Bylaws, dated June 24, 2014. Filed as Exhibit 3.2 to Current Report on Form 8-K/A filed on June 27, 2014, *available at* http://www.sec.gov/Archives/edgar/data/1031927/000141588914002003/ex3-2.htm.

While current and former stockholders are typically covered by fee-shifting provisions, this is not always the case. Biolase, Inc., which adopted a fee-shifting bylaw in connection with a dispute with a former director, adopted a provision that applies to ''any current or former director or anyone on behalf of any current or former director.'' Biolase, Inc., Section 12.2 of Sixth Amended and Restated Bylaws as of June 24, 2014. Filed as Exhibit 3.1 to Current Report on Form 8-K filed on June 30, 2014, *available at* http://www.sec.gov/Archives/edgar/data/811240/000129993314001000/exhibit1.htm. Another company adopted a clause that covers current and former stockholders as well as directors. *See* Juno Therapeutics, Inc., Article IX of Amended and Restated Bylaws, as of Dec. 2, 2014, effective Dec. 23, 2014. Filed as Exhibit 3.2 to Amendment No. 2 to Registration Statement on Form S-1 filed on Dec. 9, 2014, *available at* http://www.sec.gov/Archives/edgar/data/1594864/000119312514436942/d772541dex32.htm.

[20] *See, e.g.*, Kastis v. Carter, C.A. No. 8657-CB, Motion to Invalidate Retroactive Fee-Shifting and Surety Bylaw or, in the Alternative, to Dismiss and Withdraw Counsel at 5-6 (Del. Ch. filed July 21, 2014) (''The Bylaw imposes liability not only on stockholders but also on anyone who offers substantial assistance to the stockholders or who has a direct financial interest in a claim. Therefore, the Bylaw threatens Plaintiffs' counsel, who are prosecuting this case on a contingent basis, with liability for Defendants' fees and costs . . . . Plaintiffs and their counsel have concluded that, if the Bylaw is valid and enforceable, it would be economically irrational to continue this litigation.'').

[21] As to court oversight of fee-shifting, note that the Private Securities Litigation Reform Act of 1995 added Section 21(D)(c)(3) (Sanctions for Abusive Litigation, Presumption in Favor of Attorneys' Fees and Costs) to the Securities Exchange Act of 1934. Under that section, the court can order either side to pay fees and expenses in certain circumstances.

[22] *See supra* notes 10 and 11.

[23] *See, e.g.*, Marine Products Corporation, Amended and Restated Bylaws, dated Oct. 28, 2014. Filed as Exhibit 3.2 to Quarterly Report on Form 10-Q filed on Nov. 3, 2014, *available at* http://www.sec.gov/Archives/edgar/data/1129155/000157104914005715/ex3-2.htm.

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potential for such interest, which does not reflect true costs to an issuer, is another powerful deterrent to commencing litigation.

### No Fee Recovery for Plaintiffs

Six (15.4 percent) of the provisions state that plaintiffs and related parties must bear all of their own fees, costs and expenses, regardless of whether they are successful, and that in a derivative or class action, the claiming party is not entitled to receive any fees or expenses ''as the result of the creation of a common fund, or from a corporate benefit purportedly conferred upon the Corporation.''[24] While the language may have been crafted to address the well-known phenomenon of settlements that provide for the payment of attorneys' fees and additional SEC disclosure, but no recovery for stockholders, the language could, by itself, make it unattractive for the plaintiffs bar to even consider taking on a case.

### Tools to Enforce Fee-Shifting

Two companies require that upon request, claimants holding less than 5 percent of their voting stock post a bond covering the expenses subject to fee-shifting. While the theory may be that this prevents filing of frivolous lawsuits by stockholders who do not have ''real skin in the game,'' small stockholders with potentially valid claims will likely find it economically unfeasible to bear the additional risk of having to post a bond of unknown and potentially significant size.

### Application to Continuing Litigation

Notably, 10.3 percent (4) of the provisions analyzed specifically apply to litigation that was in effect at the time the bylaws were adopted. For plaintiffs in such a situation, the bylaw would change settled expectations and generally make it economically unfeasible to continue such litigation. Such arguments appeared to play a role in Hemispherx Biopharma, Inc. deciding not to seek enforcement of its bylaw in the context of an ongoing case.[25]

### Limitations and Severability

In recognition of potential legal challenges and the risk that certain clauses could be stricken, 71.8 percent (28) of the analyzed provisions specify that they will apply ''to the fullest extent permitted by law,'' 15.4 percent (6) include severability language and one specifies that it will not apply to the extent prohibited by the Delaware General Corporation Law. Notably, five of the severability clauses atypically provide that the bylaws should be construed to ''permit the Corporation to protect its directors, officers, employees and agents from personal liability in respect of their good faith service.''[26] Since directors, officers, and in some cases employees and agents, customarily receive such protection through indemnification provisions in the charter and/or bylaws, and directors and officers typically benefit from D&O insurance, the need for such language is debatable.

### Adopted With Exclusive Forum Clause

Reflecting the rising prominence of bylaws (and charter provisions) requiring that derivative claims and other intra-corporate disputes be litigated exclusively in a specified forum,[27] 56.4 percent (22) of the fee-shifting provisions were adopted concurrently with an exclusive forum bylaw. Both types of provisions respond to the phenomenon of strike suits brought primarily for the purpose of obtaining attorneys' fees. However, exclusive forum clauses affect where a claim is brought, not whether it may be brought. ATP-style fee-shifting provisions arguably affect whether a claim will even be brought, in light of the potential liability for a defendant corporation's expenses.

### Deemed Consent

26.4 percent (10) of the fee-shifting provisions analyzed state that stockholders are deemed to have notice of, and to have consented to, fee shifting. This language, which is common in exclusive forum provisions, appears to reflect concerns as to the enforceability of fee-shifting. However, it is not clear why such language should only apply to specific clauses, rather than the entirety of the bylaws. The same question arises in the context of exclusive forum bylaws.

### Board Waiver

Seemingly borrowing from exclusive forum clauses, 10.3 percent (4) of the fee-shifting provisions studied are elective, meaning that the board has the flexibility to waive compliance. These companies are effectively acknowledging that in some circumstances, directors may need to waive enforcement in order to satisfy their fiduciary duties.[28]

### Consent of 3 Percent of Stockholders to Sue

One corporation concurrently adopted a bylaw that prohibits any current or former stockholders or group of stockholders from initiating a direct or derivative claim ''unless the Claiming Stockholder, no later than the date on which the claim is asserted, delivers to the Secretary written consents by beneficial stockholders owning at least three percent (3%) of the outstanding shares.''[29] This is another device intended to prohibit

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[24] *See, e.g.*, Barnwell Industries, Inc., Amended and Restated Bylaws, dated Dec. 12, 2014. Filed as Exhibit 3.2 to Annual Report on Form 10-K filed on Dec. 18, 2014, *available at* http://www.sec.gov/Archives/edgar/data/10048/000110465914087562/a14-20695_1ex3d2.htm. Under the corporate benefit doctrine, a litigant who confers a significant and substantial benefit that is not monetary is entitled to an award of fees and expenses.

[25] *See supra* note 6.

[26] *See, e.g.*, Air Industries Group, Amendment No. 1 to Bylaws, dated Oct. 22, 2014. Filed as Exhibit 3.1 to Current Report on Form 8-K filed on Oct. 27, 2014, *available at* http://www.sec.gov/Archives/edgar/data/1009891/000119380514002001/e612787_ex3-1.htm.

[27] *See, e.g.*, Claudia H. Allen, *Trends in Exclusive Forum Bylaws*, The Conference Board Governance Center Director Notes, Jan. 2014, *available at* http://www.conference-board.org/governance/index.cfm?id=2439.

[28] In *Boilermakers Local 154 Retirement Fund v. Chevron Corp.*, 73 A.3d 934, 954 (Del. Ch. 2013), the seminal case upholding the validity of exclusive forum bylaws, then-Chancellor Strine noted that bylaws allowing a board to consent to jurisdiction outside the specified forum permit directors ''to meet their obligation to use their power only for proper corporate purposes.''

[29] GWG Holdings, Inc., Amendment, dated Nov. 13, 2014, to Bylaws. Filed as Exhibit 3.1 to Quarterly Report on Form 10-Q filed on Nov. 13, 2014, *available at* http://www.sec.gov/Archives/edgar/data/1522690/000121390014008040/f10q0914ex3i_gwgholding.htm.

those without ''skin in the game'' from commencing litigation.

## Conclusions

To date, fee-shifting bylaws and charter provisions have been adopted by a small number of public corporations, the majority of which are small-cap, micro-cap or nano-cap in size. While the concept of fee-shifting as a deterrent to frivolous litigation is appealing, part of the concern with provisions that hew to the ATP model is that they do not discriminate between frivolous and meritorious claims, and thus are a blunt instrument. The potential reasons that brand name companies and other large caps have not adopted this form of fee-shifting are many:

- Delaware may prohibit all or perhaps some forms of fee-shifting during the upcoming legislative session;
- If the Delaware legislature does not act, the enforcement of such bylaws will remain subject to situational review by the courts, which have yet to weigh in on enforceability;
- Several bylaws have been challenged, and one such challenge is currently pending in the Delaware Court of Chancery;
- Union and public employee pension funds have loudly voiced their disapproval, while other institutional investors have signaled significant concern;
- Many companies are unlikely to adopt a controversial provision without having discussed the issue with their largest stockholders;
- Institutional Shareholder Services, Inc.[30] and Glass Lewis & Co., LLC[31] the leading proxy advisory firms, have adopted policies generally opposing fee-shifting and may recommend ''against'' the election of certain directors, making it less likely that directors will push for adoption;
- Such fee-shifting bylaws may result in negative publicity and fiduciary litigation that in the long-run, could be more expensive than the underlying problem the bylaws seek to address; and
- Other mechanisms to deter frivolous litigation, such as exclusive forum bylaws, exist and, while not perfect, are more finely calibrated.[32]

Given these factors, it makes sense for most public companies to stop, look and listen—rather than act at this time.

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This type of bylaw was pioneered by Philip Goldstein, a principal of Bulldog Investors, who also called for such bylaws to be ratified by stockholders. *See, e.g.*, Press Release, Imperial Holdings, Inc. (Nov. 3, 2014), filed as Exhibit 99.1 to Current Report on Form 8-K filed on Nov. 3, 2014, *available at* http://www.sec.gov/Archives/edgar/data/1494448/000119312514394047/d813556dex991.htm. To date, three companies controlled by Mr. Goldstein and GWG Holdings, Inc. are the only companies known to have adopted such provisions.

[30] ISS, *United States Summary Proxy Voting Guidelines: 2015 Benchmark Policy Recommendations* (Dec. 22, 2014), http://www.issgovernance.com/file/policy/2015ussummaryvotingguidelines.pdf, stating:

> ***Unilateral Bylaw/Charter Amendments***
>
> 1.17. Generally vote against or withhold from directors individually, committee members, or the entire board (except new nominees, who should be considered case-by-case) if the board amends the company's bylaws or charter without shareholder approval in a manner that materially diminishes shareholders' rights or that could adversely impact shareholders, considering the following factors, as applicable:
>
> > The board's rationale for adopting the bylaw/charter amendment without shareholder ratification;
> >
> > Disclosure by the company of any significant engagement with shareholders regarding the amendment;
> >
> > The level of impairment of shareholders' rights caused by the board's unilateral amendment to the bylaws/charter;
> >
> > The board's track record with regard to unilateral board action on bylaw/charter amendments or other entrenchment provisions;
> >
> > The company's ownership structure;
> >
> > The company's existing governance provisions;
> >
> > Whether the amendment was made prior to or in connection with the company's initial public offering;
> >
> > The timing of the board's amendment to the bylaws/charter in connection with a significant business development;
> >
> > Other factors, as deemed appropriate, that may be relevant to determine the impact of the amendment on shareholders.

*Id.* at 12–13. In addition, ISS will generally oppose fee-shifting provisions that are put to a stockholder vote, although the policy states that such provisions will be considered on a case by case basis. *Id.* at 23–24.

[31] Glass Lewis & Co., LLC, *Proxy Paper Guidelines: 2015 Proxy Season*, http://www.glasslewis.com/assets/uploads/2013/12/2015_GUIDELINES_United_States.pdf, stating:

> We have adopted a policy regarding instances where a board has amended the company's governing documents to reduce or remove important shareholder rights, or to otherwise impede the ability of shareholders to exercise such rights, and has done so without shareholder approval. Examples of board actions that may cause such a recommendation include . . . the adoption of provisions that limit the ability of shareholders to pursue full legal recourse—such as bylaws that . . . require shareholder plaintiffs to pay the company's legal expenses in the absence of a court victory (i.e., ''fee-shifting'' or ''loser pays'' bylaws) . . . In these instances, depending on the circumstances, we may recommend that shareholders vote against the chairman of the governance committee, or the entire committee . . . .
>
> Additionally, consistent with our general approach to boards that adopt . . .fee-shifting bylaws without shareholder approval, we will recommend that shareholders vote against . . . the entire governance committee in the case of a provision limiting the ability of shareholders to pursue full legal recourse (e.g., ''fee-shifting'' bylaw), if these provisions are not put up to shareholder vote following the IPO.

*Id.* at 1–2. As a general matter, Glass Lewis ''strongly opposes the adoption of such fee-shifting bylaws.'' *Id.* at 40.

[32] On the state law level, Oklahoma enacted legislation effective Nov. 1, 2014 mandating true ''loser pays'' fee-shifting in derivative lawsuits, and allowing the court to award costs, including attorneys' fees, if the derivative action conferred a ''substantial benefit.'' *See* Oklahoma Enrolled Senate Bill No. 1799 (an act relating to derivative actions; amending 18 O.S. 2011, Section 1126), http://webserver1.lsb.state.ok.us/cf_pdf/2013-14%20ENR/SB/SB1799%20ENR.PDF.

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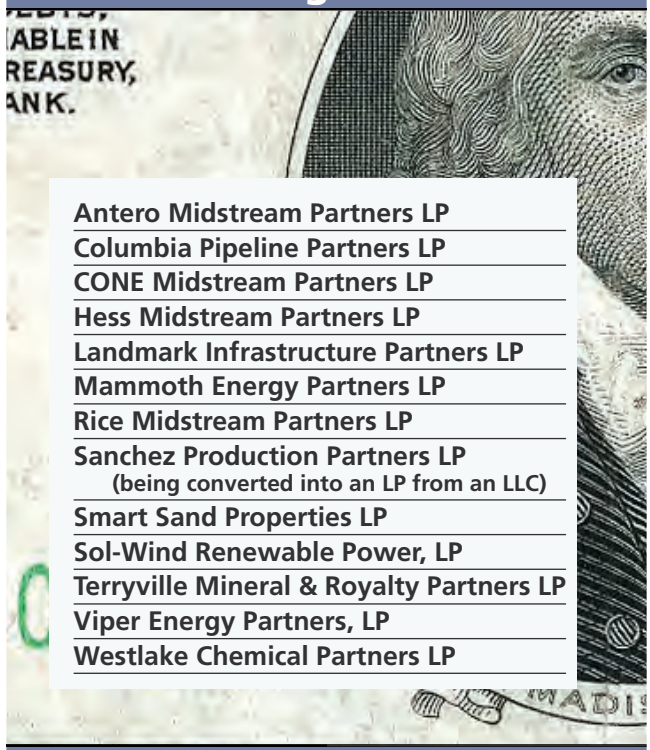
## Domestic Corporations With Fee-Shifting Provisions

- Air Industries Group
- American Spectrum Realty, Inc.
- ATD Corporation
- Barnwell Industries, Inc.
- Biolase, Inc.
- Cadista Holdings Inc.
- CIG Wireless Corp.
- Cogent Communications Holdings, Inc.
- Cryo-Cell International, Inc.
- Echo Therapeutics, Inc.
- Epiq Systems, Inc.
- FDO Holdings, Inc.
  (to be renamed Floor & Decor Holdings, Inc)
- First Aviation Services, Inc.
- Frequency Electronics, Inc.
- Freshpet, Inc.
- GAMCO Investors, Inc.
- GWG Holdings, Inc.
- Hemispherx Biopharma, Inc.
- Highlands Bankshares, Inc.
- Insys Corporation
- Interactive Brokers, Inc.
- IRADIMED CORPORATION
- Juno Therapeutics, Inc.
- KLX Inc.
- Lannett Company, Inc.
- Legacy Education Alliance, Inc.
- The LGL Group, Inc.
- Marine Products Corporation
- Mongolia Holdings, Inc.
- Nature's Sunshine Products, Inc.
- PRA Group, Inc.
  (f/k/a Portfolio Recovery Associates, Inc.)
- Riverbed Technology, Inc.
- Rocky Mountain Chocolate Factory, Inc.
- Rollins, Inc.
- RPC, Inc.
- Smart & Final Stores, Inc.
- Townsquare Media, Inc.

Source: Claudia Allen A BNA Graphic/leg012g3

[33]

## Domestic Limited Partnerships With Fee-Shifting Provisions



- Antero Midstream Partners LP
- Columbia Pipeline Partners LP
- CONE Midstream Partners LP
- Hess Midstream Partners LP
- Landmark Infrastructure Partners LP
- Mammoth Energy Partners LP
- Rice Midstream Partners LP
- Sanchez Production Partners LP
  (being converted into an LP from an LLC)
- Smart Sand Properties LP
- Sol-Wind Renewable Power, LP
- Terryville Mineral & Royalty Partners LP
- Viper Energy Partners, LP
- Westlake Chemical Partners LP

Source: Claudia Allen A BNA Graphic/leg012g4

[33] Alibaba Group Holding Ltd., a Cayman Islands entity, also adopted a fee-shifting provision. *See supra* note 12.