CLEARY GOTTLIEB

ALERT MEMORANDUM

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Selected Issues for Boards of Directors in 2014

Over the past year, boards of directors continued to face increasing scrutiny from shareholders and regulators, and the consequences of failures became more serious in terms of regulatory enforcement, shareholder litigation and market reaction. We expect these trends to continue in 2014, and proactive board oversight and involvement will remain crucial in this challenging environment.

During 2013, activist investors publicly pressured all types of companies – large and small, high-flyers and laggards – to pursue strategies focused on short-term returns, even if inconsistent with directors' preferred, sustainable long-term strategies. In addition, activists increasingly focused on governance issues, resulting in heightened shareholder scrutiny and attempts at participation in areas that historically have been management and board prerogatives. We expect increased activism in the coming year. We also expect boards to continue to have to grapple with oversight of complex issues related to executive compensation, shareholder litigation over significant transactions, risk management, tax strategies, proposed changes to audit rules, messaging to shareholders and the market, and board decision-making processes. And, as evidenced in recent headlines, in 2014 the issue of cybersecurity will demand the attention of many boards.

In light of these pressures and concerns, this memorandum reviews the following issues that we believe will require the attention of boards of directors and management in 2014:

- preparing for and responding to shareholder activism;
- potential regulatory developments involving proxy advisory firms;
- compensation plans and awards, including increasing shareholder litigation, shareholder engagement and regulatory issues;
- risk management and proposed changes to auditing and accounting requirements;
- managing board communications and processes and dealing with shareholder representatives on the board;
- the challenge of cybersecurity;
- challenges for multinationals in formulating and implementing tax strategies; and
- using forum selection clauses in bylaws and charters to manage potential shareholder litigation.

In the face of these challenges, directors should ensure that management regularly works with its advisors to monitor and adapt to the continually changing environment, and directors should participate in that engagement. For the coming year, we recommend that companies carefully track their shareholder profiles and pursue proactive approaches to potential activism. In addition, frequent and well-structured engagement with shareholders will continue to be crucial. Directors should focus on management's ability to communicate its policies and vision in a way that is understandable and convincing to shareholders and the market, and management and directors should be prepared to respond to increasing external pressures in a manner that both thoughtfully takes those pressures into account and fully reflects their carefully considered view of the long-term interests of the company.

1. Shareholder Activism – Preparing and Responding

Shareholder activism is on the rise, and recent experience has demonstrated the following:

- Activists have approached the big as well as the small (funds with as little as one or two percent of the outstanding voting power have prompted significant changes at large-cap companies);
- Strong financial results and best-practice governance do not preclude activism (steady cash flow and a healthy balance sheet are often attractive targets for activists promoting financial engineering to accelerate returns);
- Activists have significant war chests (it is estimated that activist funds control about $90 billion of capital);
- Activists can be constructive, especially after they are invited under the tent; but, once in, they can also significantly complicate board processes;
- Evolving attitudes of institutional investors have led to overt or tacit alliances between aggressive hedge funds and more passive institutional investors; and
- The influence of the proxy advisory firms, although not necessarily determinative, cannot be dismissed and must be evaluated on a case-by-case basis.

In light of these factors, directors should prepare for potential activism.

- The company should have an up-to-date strategic plan endorsed by the board.
- The company should not wait for an activist to surface to engage actively with shareholders. Preferably outside the proxy season, senior management and, if appropriate, one or more of the independent directors should explain the strategic plan to significant institutional investors, answer their questions (in compliance, of course, with Regulation FD and other disclosure rules), make clear the active role of the independent directors, listen carefully to what investors are saying, and report to the board.

- Before the activist surfaces, boards should consider what an activist likely would criticize or suggest. Directors may conclude after full analysis that there are strategies a hypothetical activist might favor that should be pursued proactively (*e.g.*, divestment of assets, spin-off of a business, increase in dividends, undertaking stock repurchases, bringing fresh voices on to the board or changing senior management). Even if this exercise leads the board to conclude that no changes are advisable, it will leave the board and the company better prepared if and when an activist delivers a letter or a "white paper," issues a press release or files a Schedule 13D.

- The company should regularly monitor changes in its shareholder makeup. If an activist surfaces – even a small investor filing a quarterly 13F – the board should be promptly informed. If the company discovers a potential activist in its shareholder profile, the board and management should immediately be briefed on:

    - Issues the activist has focused on in the past;

    - Tactics the activist has employed and the results;

    - The typical time horizon of the activist's prior investments; and

    - Legal parameters within which the activist must operate, including those arising from:

        - Charter, bylaw and state corporate law provisions governing advance notice periods for board nominations and stockholder proposals and the ability of stockholders to call special stockholder meetings or to act by written consent without a meeting;

        - Ownership limitations arising from rights plans, or that may be implemented through adoption of a rights plan that is "on the shelf" (which should be considered when an activist – alone or with other investors with similar goals – seems likely to acquire a stake of 10% or more); and

        - Other legal considerations such as antitrust or other regulatory clearance requirements or beneficial ownership reporting obligations.

Even if the board engages in every possible preparation, an activist may still surface. The actions to be taken in response to an activist will depend on the circumstances, but directors should remain mindful of the following:

- If the company is approached privately and the activist seeks a meeting, it will be advisable to meet in most instances. Disclosure of an approach or a meeting will not generally be required, but it is of course possible that the activist may go public at any time (including shortly after a meeting) and portray what is said in a negative light. In any event, the board and management should reevaluate the situation promptly following any such meeting.

- The board should be actively involved, together with management and outside advisors, in determining how best to respond to the activist, both initially and as the situation develops.

- An actual proxy contest, even one involving a "short-slate" (*i.e.*, a minority of the board seats), can be exhausting and a significant distraction from the company's business. This reality, and an honest assessment of the likely results of a contest, must be considered in deciding whether to attempt to settle with the activist and on what terms.

- Notwithstanding any distractions, management must remain focused on performance, its strategic plan and effective communications. There is no worse time to have a disappointing quarter or a failure to communicate effectively with investors about long and short-term goals.

2. Potential Regulatory Developments Involving Proxy Advisory Firms

Many companies believe that the activities of ISS and Glass Lewis pose serious governance challenges because of their significant influence on shareholders, unwillingness to engage meaningfully with companies and non-transparent methodologies. On the other hand, institutional investors vigorously assert that the proxy advisory firms perform a valuable service as it generally is not economical for the institutions to conduct the research necessary to evaluate all matters put to a vote. Numerous comment letters in response to the SEC's 2010 concept release on the proxy system focused on these issues, but there has been no significant change in the proxy advisory duopoly or the operations of the firms and no formal SEC action to regulate or monitor their activities.

We do not expect the SEC to take major action in 2014 with respect to the proxy advisory firms, but two developments in late 2013 do suggest increased attention from regulators. First, in October 2013, NASDAQ OMX filed a petition with the SEC calling for rules that would condition continued reliance on prior SEC guidance favorable to proxy advisory firms on public disclosure by the proxy advisory firms of their models, methodologies and potential conflicts of interest. Second, in December 2013, the SEC held a public roundtable on the issues. The roundtable, however, served principally as a forum where already well-established positions and arguments on the various sides of the debate were rehearsed. There were some indications of increased consensus with respect to disclosure of conflicts of interest, but much less evidence of movement regarding transparency of models and methodologies or mandated engagement with companies.

We believe that, although the SEC is attending to the issue, it is unlikely to push forward in the near term with major proposals that will deprive institutional investors of proxy advisory services they see as valuable. There is no indication that the dissatisfaction that companies express with the current situation is shared by institutional investors. This is not surprising given that institutional investors are under regulatory and other pressures to vote shares and do not (except perhaps the largest of them) have the resources to evaluate all matters on which they are asked to vote. Moreover, many institutional investors have concluded that they are better protected against challenges that their own conflicts might result in violations of their fiduciary duties if they outsource their voting decisions, even if the proxy advisory firms may have their own conflicts.

As a result, boards will need to continue to consult with their advisors regarding the most constructive approaches to advisory firms, and to follow and possibly support regulatory action in this area.

3. Compensation-Related Issues

Shareholder Litigation Regarding Compensation Plans and Awards

In 2013, there was a new cluster of shareholder cases relating to compensation – far in excess of what we have seen in the past – alleging that compensation committees misinterpreted company plans and improperly issued incentive awards without shareholder approval. The cases bring to mind the significant litigation arising from the stock option backdating scandal beginning in 2005, as some of those cases also turned on whether boards violated the provisions of their companies' plans (in those cases, provisions requiring options to be granted at not less than fair market value). Notably, these cases have led to seven rulings under Delaware law, and in general, the results have not been encouraging for companies. Four of the seven rulings permitted claims to proceed past a motion to dismiss, including two in which courts concluded that a board's interpretation "clearly violated an unambiguous provision of the plan."

However, most of these cases appear to result from hyper-technical readings of plan terms. From a planning perspective, the issues raised by these cases generally can be avoided through careful drafting of plan documents, using a less technical and more common sense interpretive approach, and appropriate skepticism and scrutiny by compensation committees of technical interpretations on which they sometimes are forced to rely.

Shareholder Engagement on Compensation

The need for most public companies to engage with shareholders regarding compensation policies and practices has been obvious for some time. Practices, however, continue to evolve, and there is no single approach that is appropriate in every case. Various factors – including the role of proxy advisors, demands by shareholders for additional influence, skepticism about the prudence of limiting compensation committee discretion, and increasing regulatory requirements – all suggest that in 2014 there will be continuing vigorous debate regarding appropriate practices without final resolution. Boards will need to continue to monitor developments and reevaluate regularly how best to communicate and engage with shareholders on the topic of compensation.

Regulatory Developments Regarding Compensation

We expect that the recently proposed CEO pay ratio rules will be finalized in 2014, and although there may still be a court challenge that delays implementation, companies and compensation committees together with their advisors will need to devote appropriate attention to computing the required numbers and crafting the related disclosures for 2015 proxy statements. In light of experience with similar types of disclosure, we believe there almost certainly will be litigation risks associated with this exercise.

Finally, many companies have implemented clawback policies ahead of the SEC's Dodd-Frank rulemaking that in some cases go beyond the Dodd-Frank requirements. This development has put some pressure on those who have not yet done so. We expect that many companies still waiting for rules may decide that it is appropriate to move in the same direction, even in the absence of SEC guidance, in order to stay in step with market practice.

4. Risk Management, Accounting and Audit Matters

In 2014, boards will be required to remain focused on issues of risk management as well as auditing processes and the integrity of financial statements. Several specific matters deserving of attention are discussed below.

Regulatory and Compliance Risk

In light of increasing regulation and enforcement, audit and risk committees should ensure that management carefully considers any changes in the company's regulatory and compliance landscape, takes appropriate steps to address those changes, and updates the board and relevant committees. Some regulatory and compliance matters, such as the Foreign Corrupt Practices Act, have broad applicability to many companies, but others are more narrowly targeted and require management, boards and committees to evaluate carefully the circumstances and regulatory issues applicable to their particular situation. As part of their oversight functions, boards and committees should consider how to obtain sufficient comfort that the company has appropriate written policies and training programs, programs to encourage the use of internal channels to bring complaints and problems to the company's attention, whistleblower procedures and proper "tone at the top."

Proposed Changes to the Auditor Reporting Model

The Public Company Accounting Oversight Board, or PCAOB, has proposed new auditing standards requiring additional information in audit reports. That information would include, first, a discussion by the auditor of "critical audit matters," which are the aspects of the audit requiring the most complex determinations, the most professional judgment and similar elements, and, second, specific statements by the auditor regarding whether, following its evaluation of information obtained in the audit, the information in the company's filing outside the financial statements contains material misstatements or material inconsistencies with the financial statements.

If adopted, these changes will result in disclosure by auditors of information, such as information about internal controls, that until now was a disclosure decision made by companies themselves. They will also increase costs of the audit and will almost certainly adversely impact openness of communications among management and audit committees and auditors. The comment period for these rules has just closed, no new standards have yet been adopted, and any new standards would be subject to SEC approval. However, audit committees and CFOs should proactively engage with their outside auditors to determine in general terms how the proposals are likely to impact the audit, the company's audit report and relations between the auditor and the audit committee and management. Subjects for discussion could include a preliminary understanding of what critical audit matters might be identified for a particular company, what additional company information might be most likely to be disclosed in the auditor report, and how the auditor might proceed to consider information outside the financial statements.

Auditor Rotation

The PCAOB also continues to consider a new standard regarding mandatory auditor rotation. While there is no specific proposal on the table, audit committees should make sure they are kept up-to-date on any developments in the area. Recent action in the European Union to move to a 10-year rotation system may increase pressure on the PCAOB. In addition, the possibility of such a standard makes it more important for audit committees and financial management to consider on a periodic basis whether there is another firm with suitable qualifications that is independent under SEC and PCAOB rules if a change in auditor were to be required.

5. Cybersecurity Issues

Cybersecurity breaches are now a common occurrence, and the significant consequences of breaches have been widely reported. In 2014, issues of cybersecurity should be considered not only from the IT perspective but also as a matter of risk assessment and management for boards of directors.

While potential legal liability is an important driver of developing a robust cybersecurity risk program, the operational, financial, reputational and other risks may be even more serious. The recently highlighted legal risks include violations of privacy laws for disclosure of personal information, violations of disclosure requirements (as emphasized in an SEC release in 2011) if breaches result in material financial or business consequences, and FTC enforcement with respect to breaches that result in compromising customer information. The considerable risks beyond the legal sphere involve business interruption, lock-outs of customers from companies' networks and services, business and financial losses if information is compromised, and reputational damage, including loss of trust among customers and others, which can result in consequences that are significant and that can be of much longer duration than the actual breach. While risks vary by company, no public company should conclude that the probability and consequences of a cybersecurity breach are so inconsequential that consideration at the board level is unnecessary.

Boards first should consider – directly or through their audit or risk committee – measures such as the following to establish appropriate oversight:

- Instructing senior management to ascertain the particular kinds of cybersecurity risks to which the company is subject;
- Requiring senior management to develop and report on a plan that addresses cybersecurity risks, including identifying and if necessary hiring personnel with not only IT but also security and risk management skills;
- Delegating to appropriate board committees oversight of the most important cybersecurity risks and arranging for full board awareness of and engagement in these oversight efforts; and
- Ensuring periodic reporting to the audit or risk committee or the board of the status of cybersecurity risk assessment and how the risk is managed by senior management and the responsible personnel.

Beyond the steps to establish an oversight framework, boards should consider proactive steps in the following additional areas:

- *Working with senior management to understand risk and risk tolerance*. Although "zero tolerance" might seem attractive, in fact assessing and managing most aspects of cybersecurity risk involves a calculus of the risk involved in various business strategies and operations. For example, distributed IT resources increase the risk of breach, but that risk has to be assessed against the business advantages to a particular company of use of remote and other distributed devices.
- *Implementing a rapid response program to address breaches*. The board or the appropriate committee should satisfy itself that management has in place the resources and processes necessary to respond to a breach. This requires identifying privacy and security concerns, and selecting law firms to deal with legal issues involving disclosure and data privacy and security, experts to assist in investigating and analyzing the breach and its consequences, public relations or government relations firms and the internal team that will be in charge of coordinating and executing the response.

- *Using internal audit to evaluate cybersecurity weaknesses.* Audit committees should be charged with ensuring that the internal audit function is risk-based and addresses cybersecurity risks with appropriate frequency and in appropriate depth. Doing so involves not only focus on IT, but also emphasis on cybersecurity issues within the overall IT area. For example, many of the most frequently reported breaches involve use of unauthorized access, stolen passwords and the like. Therefore, internal audits of various IT functions should pay due attention to such mundane areas as expired, unauthorized or overly broad access and password protection.

- *Cybersecurity concerns do not stop at the water's edge*. For global companies, cybersecurity is a global concern. Boards should take necessary steps to be satisfied that offshore operations, processes and data are subject to the same protections and contingency plans as those put in place domestically. Companies should also be aware of the different legal implications of breaches in different jurisdictions. For example, breaches that compromise personal information of customers or others can trigger different and more exacting reporting and other consequences in the European Union than in the United States.

- *Responsiveness to cybersecurity concerns as an element of board composition*. If directors feel that the board lacks necessary expertise with respect to cybersecurity issues, nominating committees and boards should consider cybersecurity expertise as part of evaluating board composition and identifying candidates for board succession. In addition to IT skills, boards should consider regulatory experience and experience providing oversight in crisis situations, including overseeing coordination of different response teams and internal, government and external communications.

6. The Changing Tax Environment for Multinationals

Over the past few years there have been major changes in the global tax environment for multinational companies. As a result, it is advisable for boards in overseeing business strategy to monitor whether the company's cross-border tax strategies make it vulnerable to criticism or audit risk.

- *Tax audits.* Tax authorities increasingly have been instituting high-stakes investigations and challenges to the techniques used by multinationals to reduce their effective tax rate by eroding the tax base in high-tax countries and shifting profits to low-tax countries. In Europe, some of these investigations have been quite aggressive, including criminal prosecution of executives.

- *Media and political attention.* Government activities to address base erosion and profit-shifting (or "BEPS") have also resulted in damaging media coverage, governmental reports, and congressional and parliamentary hearings, including the "naming and shaming" of companies. The resulting public and political indignation at the low effective tax rate of many multinationals has fueled further audits and given rise to proposals for changes in law.

- *Potential changes in law.* There is now a concerted effort by the Organization of Economic Cooperation and Development (the "OECD") and the G-20 governments to develop and implement a harmonized international approach to address BEPS. The OECD has announced an ambitious action plan targeting many of the perceived weaknesses in current international tax rules. While the ultimate outcome is still unclear, it is likely that over time at least some major changes will result.

Consequently, boards of directors and audit committees of multinational companies may need to devote increased attention to cross-border tax risks. Depending upon the circumstances, a board might consider a focused review of international tax strategy, country-by-country effective tax rates, the level of reserves and potential exposures for past and current practices, accounting for uncertain tax positions, and potential changes in tax law. Directors should also become informed about the company's processes for developing and implementing global tax strategy, and whether it takes account of the changing tax environment in a manner that is consistent with the company's overall risk profile. Tax law developments in response to BEPS may also necessitate modifications to business practices and an evaluation of the impact of these changes on the company's effective tax rate.

7. Managing Board Communications and Stockholder-Representative Directors

Over the past year, counsel to plaintiffs in derivative and stockholder suits as well as activist investors with representatives on boards have become increasingly aggressive in trying to increase access to confidential board materials, including by seeking to challenge attorney-client privilege These developments are consistent with trends to open up board processes and enhance the roles of directors representing activist stockholders. Considerations for boards and general counsels to keep in mind in connection with board processes going forward include the following:

Use of E-mail and Board Portals

Despite the increased use of board portals, many directors still prefer to receive materials via e-mail. This raises a variety of concerns. In particular, materials sent to a director at an e-mail address at another company might give the other company access to those emails through its employment or other policies. This third-party access has provided a basis for recent claims that there has been a waiver of any privilege. An express written understanding with the other company that e-mails to the director in his or her capacity as such will be exempt from this access policy will be a helpful defense against such a claim.

Sending materials to a director at a personal e-mail address, to which third parties do not have access, avoids this issue of privilege waiver; but, if the board e-mails are mixed in with personal e-mails of the director (as opposed to being segregated), then the director will be vulnerable to having personal e-mails subject to review in connection with discovery.

Board portals can avoid these risks, but they present their own potential pitfalls. In setting up a board portal, companies should be aware that data that tracks directors' activity (or lack thereof) on a board portal may be discoverable. Moreover, some portals permit directors to make comments on materials that may be discoverable. These features should be addressed through document retention policies specific to the portal.

Finally, access to certain materials on the portal may have to be limited. For example, materials for a committee of disinterested directors will typically need to have limitations on access for those not on the committee (including in some cases management and the general counsel) to preserve privilege, as well as the integrity of the committee. Similar issues are raised in the case of an adverse dissident director, as discussed below.

Privilege and Confidentiality When a Director Becomes Adverse

A claim of privilege against a director is not generally permitted in respect of materials prepared by counsel to a board. There is an important exception when the director in question assumes a position that is "adverse" to the board. However, a claim of privilege against such a director is generally not permitted in respect of materials prepared before counsel becomes aware that the director has become adverse. This past year, dissident directors, representing activist funds, took advantage of these limitations on assertion of privilege to obtain favorable rulings in discovery proceedings. As a result, dissident directors obtained access to not only communications by counsel to the other directors, but also internal communications of counsel to the board or committee of which the dissident director had been a member. Directors and their advisors should be mindful to avoid falling into the trap of prematurely concluding that a director is adverse. Differing viewpoints and "behind the scenes" tension may be inadequate to establish the adversity necessary to entitle materials and communications to a claim of privilege against a director notwithstanding the belief at the time of the creation of these materials and communications that a true adversarial relationship is inevitable.

Access Beyond the Director for Stockholder Representatives

Further compounding the consequences for access in contexts where a director is not yet "adverse," but may become so, is the growing acceptance by courts of the premise that, when a director affiliated with a stockholder serves on the board as a "representative" of this stockholder (such as an activist fund), the company should understand that the director will be sharing confidential board materials with the stockholder (*i.e.*, the investment committee at the fund and perhaps even the fund's advisors and expert consultants) for use in conformity with the restrictions (*e.g.*, insider trading rules) applicable to the director. This presumed access by the stockholder to the board's confidential materials may have unexpected consequences if the fund has principals with fiduciary duties of candor to boards at other companies or entities for which this confidential information may be material. Directors who are affiliated with a stockholder and serving on the board as "representatives" of this stockholder, as well as the general counsels of companies with such directors on their boards, need to be proactive to assure that access to confidential board materials does not lead to an awkward "dual fiduciary" situation for these directors, the stockholder they "represent," and these companies.

In 2014, we expect activist stockholders, which have their principals or employees serving as their representatives on boards, to continue to push for obtaining more information, including by (a) resisting requirements to enter into confidentiality undertakings that extend beyond those applicable to directors generally and (b) asserting their rights to sufficient advance notice of meetings and board materials and access to confidential materials of the company beyond those provided in the board "pre-read" materials (or packages).

To counter this push, companies in 2014 will likely be considering ways to limit the influence of directors with financial ties to activist stockholders by highlighting the risk that these directors' incentives, which are created by their financial arrangements with activist funds, may cause their views to diverge from the best interests of stockholders generally. These efforts will range from mechanics (such as bylaw amendments) to exclude these directors from serving on the board altogether to determinations by boards in specific scenarios to exclude these directors from playing central roles in strategic decision-making and special committees. But even conflicted directors will continue to be entitled to access to confidential information of the corporation and it is unlikely that that they can be prevented from making public statements that they believe in good faith are consistent with their fiduciary duties.

8. Forum Selection Clauses to Limit Stockholder Litigation

In 2013 Delaware's Chancellor Strine decided, in cases involving Chevron and Federal Express,[1] that bylaws of Delaware companies could validly select Delaware courts as the exclusive forum for litigation of internal corporate affairs, such as derivative claims and mergers. These decisions are a helpful remedy to the epidemic of such litigation, and in particular to its manifestation in the form of lawsuits filed in multiple courts, a development that has also reached epidemic proportions. In 2012, 96% of public company mergers valued in excess of $500 million generated judicial challenges by stockholders seeking to enjoin them, and in the overwhelming number of cases there were multiple such lawsuits filed in multiple courts. Absent forum selection clauses, defendants have limited, and generally ineffective, tools to consolidate such cases.

The next chapter in forum selection clauses will focus on judicial receptivity. For Delaware, the answer is known. But the true test will be how quickly and effectively defendants can obtain the dismissal of cases filed outside of the selected exclusive forum. The answer is still unclear as such clauses have not been sufficiently tested in courts outside Delaware.

One powerful way to enhance the effectiveness of forum selection clauses is to include language in them whereby stockholders consent (a) to the jurisdiction of the selected forum with respect to the enforcement of those clauses and (b) to simple means of effecting service of process on any stockholder who commences litigation covered by the clause outside of Delaware. Our memorandum of November 19, 2013 sets forth model bylaw language. Together, these provisions should enable defendants to seek relief from the selected forum, in the form of a final judgment that should be backstopped by the Full Faith and Credit Clause of

[1] *Boilermakers Local 154 Retirement Fund et al. v. Chevron Corp. et al.*, *IClub Investment Partnership v. FedEx Corp. et al.* (Del. Ch. June 25, 2013).

the Constitution. As a result, the risk and uncertainty of a foreign court permitting an action to go forward in violation of an exclusive forum clause should diminish – probably, dramatically so.

Widespread adoption of forum selection clauses (coupled with jurisdictional consent/service provisions) likely will have important effects beyond just diminishing the wasted expense of having to defend essentially the same lawsuit before multiple courts. First, there is good reason to believe that many suits brought only outside of Delaware would not be brought at all if they could only be filed in Delaware. Many cases are filed outside of Delaware because there is little chance that they would survive in Delaware's courts. Second, with fewer cases being filed outside Delaware, certainty and predictability become more likely, since Delaware law will be "made" by essentially a single trial level court, and overseen by a single appellate court. Third, diminishing the likelihood of multiple courts hearing the same case reduces incentives, such as so-called "reverse auctions" where defendants play one set of plaintiffs against another in order to secure the cheapest settlement (which, in some instances, may be beneficial to defendants). On the other hand, if (ex ante) companies would prefer a jurisdiction other than the state of incorporation to be the exclusive forum, clauses so providing should be valid in many, if not all, jurisdictions, so long as the selected jurisdiction has a reasonable connection to the corporation (e.g., where it is headquartered).

Since the Chevron/FedEx decisions in June 2013, boards of over 150 listed companies have amended their bylaws to adopt forum selection clauses and the number of companies adopting such clauses in their charters or bylaws at the time of their IPO or other initial listing is increasing. Other public companies have been deterred by the attitudes of the major proxy advisory firms and some institutional investors. The advisory firms take the position that amending bylaws to adopt such a provision should not be done without a shareholder vote. Each company and its board must make its own decision in light of its shareholder profile, policies and attitudes of institutional shareholders as well as ISS and Glass Lewis and other factors, but there are real benefits to shareholders of eliminating overlapping lawsuits in multiple jurisdictions that the company and its board must defend, and it is to be hoped that over time, as more companies adopt such provisions, some of the negative reaction will lessen.

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Please call any of your regular contacts at the firm or any of the partners and counsel listed under Capital Markets, Corporate Governance, Executive Compensation, Mergers and Acquisitions or Tax in the Practices section of our website (www.cgsh.com) if you have any questions.

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