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ALERT MEMORANDUM

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Enhancing the Promise of Exclusive Forum Clauses by Having Stockholders Consent to the Jurisdiction of the Selected Forum

The multiplicity of cases brought on behalf of the same stockholder group (or as derivative actions) against the same defendants based on the same conduct and asserting the same fiduciary duty claims is now well documented. The benefits of consolidating such litigation in a single forum have also been well established.

Most such litigation takes place in state courts, particularly where the litigation concerns transformative corporate events like mergers. Within the federal system, there is a specialized tribunal – the Judicial Panel on Multidistrict Litigation – charged with allocating business among the different federal district courts when the same or similar cases are pending in several such courts. There is nothing similar, however, in the state court systems that can allocate cases among courts of different states.

In the recent Chevron/Federal Express decision, Chancellor Strine found to be valid under Delaware law a bylaw provision designating Delaware as the exclusive forum to hear internal affairs claims involving Delaware companies. Unless overturned on appeal, Delaware companies are accordingly now able to reduce the transactional and related costs of multi-forum litigation of the same case by adopting provisions in organic corporate documents selecting an exclusive forum (presumably, Delaware) where internal corporate affairs disputes can be heard.[1]

But the real test of these provisions will be whether they are respected by courts outside of the state of incorporation. They should be. It is a well-accepted principle of conflicts of laws jurisprudence that the substantive law of the state of incorporation applies to internal affairs disputes, and courts outside of the place of incorporation are expected to faithfully apply it. Nevertheless, whether (and if so, how quickly) this will come to pass is at best unclear.

Powerful economic interests have led to virtually every merger valued in excess of $500 million (96% in 2012) being challenged by stockholder plaintiffs, who file suits outside the target company's state of incorporation (whether or not suits are also filed in that state) almost 85% of the time. Despite the Chancellor's thoughtful and compelling opinion, it is likely that some plaintiffs will bring internal affairs claims in "foreign" courts and seek to convince those courts to reject the applicability or validity of forum selection clauses. One can imagine arguments, for

[1] Under Chancellor Strine's reasoning, exclusive forum clauses can likely be validly adopted by companies chartered under the corporate law of other states (the relevant state corporation law, however, would of course need to be reviewed).

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example, that the exclusive forum clauses are procedural rules that affect how (or more specifically where) lawsuits are brought and should therefore yield to statutes or common law policies that, for example, atmospherically or otherwise favor retaining cases in the "foreign" court (for example, in a state where the named plaintiffs are residents or the defendant corporation is headquartered). Such statutes and policies often frustrate (or outright preclude) efforts to dismiss or stay cases under the *forum non conveniens* doctrine, which is the primary method (in the absence of an exclusive forum clause) for channeling intra-corporate internal affairs claims into a single state forum. In the long run, those arguments should not be successful, but they will likely be tried, as may others.[2] Moreover, boards may have discretion under forum selection clauses to waive the exclusivity of the forum selected in the clause – leaving room for the possibility that there may be circumstances where, in the exercise of their fiduciary duties, board members may deem it appropriate for a litigation to proceed outside of the selected forum. Motivated stockholder plaintiffs who file suit in foreign courts may seek to exploit this "fiduciary out," contending that invoking the forum selection clause in the particular circumstances of a given case would itself violate a board's fiduciary duties and that the initial decision should not itself be subject to the exclusive forum clause. Thus, until the decisional law outside of Delaware (or other state of incorporation) accepts the validity of exclusive forum clauses, and the circumstances become well-defined where fiduciary duties require suits outside of the selected forum to continue there, the very uncertainty and inefficiencies that forum selection clauses are designed to address will to a meaningful degree remain.

Issuers considering adopting an exclusive forum clause – a provision providing that claims involving a corporation's internal affairs can only be brought in specified courts[3] – should consider the potential benefits of including a related provision that stockholders are deemed to consent to the personal jurisdiction of such courts with respect to actions to enforce such clauses.

The same analysis that supports the validity of a forum selection clause should also support the validity of a jurisdictional consent clause. Because, as Chancellor Strine held, Delaware law permits bylaws to include forum selection clauses that bind all shareholders, jurisdictional consents permitting those clauses to be enforced against shareholders in the selected courts should also be valid. Further, since consent is a well-recognized basis for conferring personal jurisdiction, the same mechanism that is sufficient to confer consent to a forum selection clause should also satisfy any due process requirements for conferring personal jurisdiction for the purpose of enforcing them.

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[2] Indeed, in the one instance where a foreign court was presented with a forum selection clause, it refused to enforce it – though this was before Chancellor's Strine's explication of Delaware law.

[3] See our June 27 memorandum, "Should Your Company Accept A Forum Selection Bylaw?," on relevant considerations with respect to the adoption of forum selection clauses. http://www.cgsh.com/should-your-company-adopt-a-forum-selection-bylaw/

Jurisdictional consent provisions would have the limited, but powerful, effect of permitting the corporation or affected fiduciaries[4] – the defendants in the foreign forum – to bring suit in the exclusive forum, and litigate there the enforceability of the exclusive forum clause. Thus, to the extent litigation is brought in violation of the exclusive forum clause, the company or the defendant fiduciaries need not go to the foreign court to enforce the clause; rather, they can bring suit for a declaration and injunction in the court selected in the clause against the plaintiff in the foreign court, directing that the stockholder plaintiff dismiss the foreign action. A permanent injunction in such a proceeding should be entitled to full faith and credit in any court in the United States. Such injunctions would likely be quickly granted as the issues are straightforward and determined by the forum selection clause itself, and the nature of the claims asserted in the foreign court as set forth in the relevant pleading. If the stockholder plaintiff in the foreign court chooses to appear and defend the forum selection clause enforcement case, then jurisdiction over him in that court is unquestionably established. And if he defaults, the only open questions would be whether there is such jurisdiction in the selected state under the law of that state and, if so, whether the exercise of such jurisdiction is constitutional – questions that do not implicate policies such as those hostile to *forum non conveniens*.

Once the validity of exclusive forum clauses gains widespread acceptance, the rationale for jurisdictional consent clauses may be largely eliminated. Until then, though (and perhaps thereafter as well), the promise of reducing the costs, inefficiencies, and potential of conflicting rulings provided by exclusive forum clauses will likely be enhanced and accelerated by the adoption of jurisdictional consent clauses.

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[4] Corporations or directors likely will not bring claims against stockholders lightly, if for nothing else than reputational reasons. That said, the only potential stockholder defendants in forum selection clause enforcement proceedings would be those who have already violated that clause and brought suit elsewhere against the corporation or its fiduciaries. Moreover, such clauses can be drafted also to permit other stockholders (such as those who have brought similar suits in the proper forum) to utilize such consent to jurisdiction to enforce the forum selection clause.

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