

## INSIGHTS

## Delaware Court Approves Out-Of-State Forum Selection Bylaw Adopted At Time Of Merger

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In *City of Providence v. First Citizens BancShares Inc. et al.*, C.A. No. 9795-CB (Del. Ch. Sept. 8, 2014), the Delaware Court of Chancery (Bouchard, C.) held that a minority shareholder's claims against a Delaware corporation's controlling shareholder and board of directors must be litigated in North Carolina based on a forum selection bylaw (the "Forum Bylaw") that designated North Carolina as the exclusive forum for litigation, even though it was adopted the same day a merger was announced. Relying heavily on *Boilermakers Local 154 Retirement Fund v. Chevron Corporation* ("Chevron"), 73 A.3d 934 (Del. Ch. 2013), an opinion authored by former Chancellor Strine shortly before he became Chief Justice of the Delaware Supreme Court, the Court held that the Forum Bylaw was facially valid and enforceable, and that the timing of the board of directors adoption of the Forum Bylaw was immaterial absent allegations sufficient to rebut the business judgment rule.

### Case Summary

The lawsuit arose after the board of directors (the "Board") of defendant First Citizens BancShares, Inc. ("FC North"), a company incorporated in Delaware with its principal place of business in North Carolina, approved and adopted a bylaw that designated the federal and state courts of North Carolina as the exclusive jurisdiction for litigation against the company and its directors, officers, and employees asserting (i) any derivative claim; (ii) any claim for breach of fiduciary duty; (iii) any claim arising under the Delaware General Corporation Law; and (iv) any claim governed by the internal affairs doctrine. Slip Op. at 1, 3, 7-8. That same day, FC North announced its acquisition of First Citizens Bancorporation, Inc. ("FC South") (the "Merger"). Slip Op. at 1, 3. FC North and FC South allegedly were under the common control of the Holding family (the "Holding Group"). Slip Op. at 3.

On June 19, 2014, the City of Providence ("Plaintiff") filed the first of two complaints, which later were consolidated. Slip Op. at 3. The first complaint (the "Bylaw Complaint") asserted claims against FC North and its Board members seeking, *inter alia*, to invalidate the Forum Bylaw and alleging that its adoption was a breach of fiduciary duty. Slip Op. at 3-4. On August 1, 2014, Plaintiff filed its second complaint (the "Merger Complaint") asserting, *inter alia*, class and derivative claims for breach of fiduciary duty against controlling shareholder the Holding Group and the Board for approving the Merger, which allegedly was designed to deliver excessive shares to the Holding Group and to decrease the voting power of minority, public shareholders. Slip Op. at 4. On August 28, 2014, Plaintiff filed a motion to expedite and enjoin a September 16, 2014 vote by FC North's shareholders on various issues related to the Merger. Slip Op. at 5.

The defendants moved to dismiss both complaints. Slip Op. at 4. The Court granted the motions, holding that the Forum Bylaw was facially valid and enforceable, that the Board had not breached its fiduciary duties by adopting it, and thus that Plaintiff's merger-related claims should be litigated in North Carolina. Slip Op. at 1-2, 4.

### **The Court's Reasoning**

The threshold issue before Court was whether the Forum Bylaw was enforceable. The parties agreed that the Forum Bylaw governed the claims asserted in the Merger Complaint, and, therefore, stipulated that the enforceability of the Forum Bylaw should be resolved prior to reaching Plaintiff's Merger-related claims. Slip Op. at 5.

The Court first noted that FC North's charter authorized the Board to amend the corporation's bylaws. Thus, as the Court had reasoned in *Chevron*, FC North's shareholders had assented to a framework that explicitly authorized the Board to adopt bylaws unilaterally. Slip Op. at 7, 9. The Court described the Forum Bylaw as "functionally identical" to the bylaw at issue in *Chevron*, except it selected North Carolina, rather than Delaware, as the exclusive forum. Slip Op. at 7. The Court reasoned that "nothing in the text or reasoning of *Chevron* can be said to prohibit directors of a Delaware corporation from designating an exclusive forum other than Delaware in its bylaws." Slip Op. at 10. Thus, the Court held that the fact that FC North selected North Carolina as the exclusive forum "[did] not...call into question the facial validity" of the Forum Bylaw, particularly because North Carolina is "the second most obviously reasonable forum given that FC North is headquartered and has most of its operations there." Slip Op. at 10.

The Court next addressed the Plaintiff's assertion that the Board's "self-interested" adoption of the Forum Bylaw constituted a breach of its fiduciary duty. Slip Op. at 13. The Court rejected this argument, finding it to be "wholly conclusory." Slip Op. at 13. The Court explained that the Forum Bylaw "plainly does not insulate the Board's approval of the proposed merger from judicial review. It simply requires that such review take place in a court based in North Carolina." Slip Op. at 13. As a result, Plaintiff "failed to rebut the presumption of the business judgment standard of review that attaches to the Board's adoption of the [Forum Bylaw] or to show that the Board's selection of North Carolina as the exclusive forum was irrational." Slip Op. at 14.

Finally, the Court turned to Plaintiff's three arguments regarding whether the Forum Bylaw was valid as applied to the facts alleged in the Complaint. Plaintiff first argued that Delaware had an overriding interest in applying its law to the "novel and substantial" issues raised by the Merger Complaint. Slip Op. at 16. The Court rejected Plaintiff's contention, finding Plaintiff overstated the novelty of its claims and that it discerned no "overarching public policy of this State that prevents boards of directors of Delaware corporations from adopting bylaws to require stockholders to litigate intra-corporate disputes in a foreign jurisdiction." Slip Op. at 19.

Second, Plaintiff asserted that it would be unreasonable, unjust and/or inequitable to enforce the Forum Bylaw because it occurred simultaneous with the Merger announcement and because of the related-party nature of the Merger. Slip Op. at 17, 20. The Court rejected this argument, again citing *Chevron* for the notion that "the reasonable expectation a stockholder of FC North should have is that its Board may adopt a forum selection bylaw that, subject to challenge on an as-applied basis, designates a court outside Delaware as the exclusive forum for intra-corporate disputes." Slip Op. at 20-21 (citing *Chevron*, 73 A.3d at 940). The fact that the Forum Bylaw was adopted "on an allegedly 'cloudy' day when it entered into the merger

agreement...rather than on a 'clear' day [was] immaterial given the lack of any well-pled allegations in either of Plaintiff's [complaints] demonstrating any impropriety in this timing," Slip Op. at 21. Likewise, the Court concluded that the related-party nature of the transaction did not render it inequitable to enforce the Forum Bylaw. The Court emphasized the absence of any allegations that the Board selected North Carolina for an improper purpose, and that the Forum Bylaw did not absolve the Board's conduct from judicial review, but merely mandated that judicial review take place in North Carolina. Slip Op. at 21.

Third, Plaintiff argued that it would be unjust to apply the Forum Bylaw because FC North's shareholders could not repeal it due to the Holding Group's control of the company. Slip Op. at 22. The Court rejected this claim, stating that a controlling shareholder's support of a bylaw, in and of itself, "does not make it *per se* unreasonable to enforce." Slip Op. at 23. Indeed, finding to the contrary would call into question all board-adopted bylaws of controlled corporations. Slip Op. at 23.

### **Takeaways**

While this is not the first Delaware Court of Chancery case to approve an exclusive forum selection bylaw, it is notable for at least two reasons. First, it opens the door for Delaware corporations to adopt forum selection bylaws designating exclusive jurisdiction in states other than Delaware. Such clauses may be especially attractive for corporations such as FC North, which are incorporated in Delaware but based in, and operated out of, another state.

Second, the decision establishes that absent sufficient allegations to rebut the business judgment rule, a board can enact a forum selection bylaw in connection with an M&A transaction for the purpose of eliminating the possibility of multi-forum litigation arising out of that transaction. Indeed, as the Court recognized, "[t]he whole point of adopting the [Forum Bylaw] was to solve the issue of multi-forum litigation such that this Court (and courts in other jurisdictions) would not need to divine the appropriate forum." Slip Op. at 18. Further, the timing of a board's adoption of a forum selection bylaw is immaterial absent allegations that the timing was based on an improper reason or purpose, and the adoption of such a clause may be permissible even where the M&A transaction involves a controlling shareholder.