

Corporate accountability suffered a surprising blow earlier this year when the Delaware Supreme Court allowed corporate boards to eliminate an important safeguard of investors' rights: the private enforcement of meritorious state and federal securities laws.

In *ATP Tour, Inc., et. al. v. Deutscher Tennis Bund (ATP Tour)*, the Court held that corporate boards of directors are free to unilaterally adopt bylaw provisions that may essentially grant themselves immunity from being held legally accountable by shareowners. The May 8 decision has ignited a new "race to the bottom" as some corporations – and even some state legislatures – have begun to adopt increasingly extreme provisions and enact laws that restrict shareowners' ability to bring claims against, or on behalf of the companies in which they invest.

In *ATP Tour*, the Court held that ATP was free to adopt a one-sided fee-shifting bylaw without shareholder approval. This provision requires that an investor bringing a claim against ATP must substantially achieve, in substance and amount, the full remedy sought, or else that investor will have to pay all of ATP's legal expenses. When faced with such extreme fee-shifting bylaws, many rational investors would opt to abstain from pursuing meritorious litigation if winning on most, but not all counts, could result in the investor being forced to incur material financial obligations to a company that was shown to have engaged in wrongdoing.

The Council of Institutional Investors (CII) opposes fee-shifting provisions because they establish a structure that significantly deters or eliminates meritorious shareowner claims, thereby eliminating a company's accountability to its owners, an important safeguard to ensure good corporate governance.

Fee-shifting provisions may amount to a tacit grant of immunity because not even some of the largest institutional investors will risk depleting their assets to hold a corporate board accountable in court. The implications on corporate accountability can be enormous: By eliminating investors' ability to enforce state and federal securities laws, it will become more difficult to prevent and remedy corporate fraud and unlawful conduct.

In response to the *ATP Tour* decision, the Corporation Law Section of the Delaware State Bar and the Delaware General Assembly advanced a bill clarifying that, unless permitted by statute, "neither the certificate of incorporation nor the bylaws of any [stock] corporation may impose monetary liability, or responsibility for any debts of the corporation, on any stockholder."

As this bill was being considered in June, CII urged Delaware lawmakers to act promptly to preempt corporate boards from adopting these one-sided, fee-shifting bylaws, ultimately eroding commitments to good corporate governance. As we stated in our letter: "The proliferation of so-called 'fee-shifting bylaws' that could result from the *ATP Tour* decision would reduce, rather than protect and enhance, a corporation's accountability to shareowners."

Unfortunately, after intense lobbying by special interest groups that support immunity-granting provisions, the Assembly decided to delay a vote on the bill until the next legislative session. Since that time, dozens of public companies have adopted either bylaws or charter provisions mandating that an "unsuccessful" plaintiff in shareowner litigation must pay the fees and expenses of all defendants. Delaware's legislature will have the opportunity to restore critical investor protections when it returns in January.

Last week, CII again called on Delaware lawmakers to act in the in the interest of investors and preserve Delaware's position as a fair forum for businesses. At the same time, a coalition of institutional investors, representing nearly \$2 trillion in assets also reached out to Delaware lawmakers demanding that they restore investors' legal rights and ensure good corporate governance. Those institutional investors,

including CII members representing retirement funds for millions of current and retired teachers, first responders, and government employees, made clear the dire need for immediate legislative action, stating in their letter:

“These bylaws effectively make corporate directors and officers unaccountable for serious wrongdoing. The General Assembly must act promptly to restore confidence in Delaware’s credibility in developing a balanced corporate law, preserve stockholders’ access to the court system, and make clear that directors and officers cannot insulate themselves from accountability under the guise of unilateral bylaw or charter provisions.”

Legislative measures must be pursued vigorously to overturn or narrow the scope of the *ATP Tour* decision. Unless these immunity-granting provisions are thwarted, the responsibility of corporations to their investors will decline as corporate officials who commit wrongdoing will become more insulated from legal accountability, potentially threatening the financial security of shareowners and our capital market system.

Jeff Mahoney  
General Counsel  
Council of Institutional Investors  
Washington, DC  
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