U.S. CHAMBER
Institute for Legal Reform

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Norman Monhait
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Dear Mr. Monhait:

This letter is submitted on behalf of the U.S. Chamber Institute for Legal Reform ("ILR"). The U.S. Chamber of Commerce (the "Chamber") is the world's largest business federation, representing the interests of more than three million companies of every size, sector, and region. ILR is an affiliate of the Chamber dedicated to making our nation's overall civil legal system simpler, faster, and fair for all participants.

I am writing with regard to the Corporation Law Council's proposal, released on March 6, to bar stock corporations from adopting fee-shifting bylaws or charter provisions, and to expressly authorize adoption of forum-selection bylaws.

We are extremely concerned that this proposal, if adopted, would eliminate an important mechanism that corporations have turned to in order to protect innocent shareholders against the significant costs of abusive litigation without providing an adequate replacement tool—either to corporations or to the Court of Chancery—to deter the filing and prosecution of these illegitimate actions. Particularly in light of the proposal's validation of forum-selection bylaws, which we support, Delaware must address the substantive problem of abusive lawsuits, which are now likely to become centralized in Delaware's courts.

ILR and the Chamber have long been concerned about the well-documented, widespread abuse in connection with lawsuits challenging merger and acquisition transactions. In 2012, ILR released a detailed study of the issue entitled *The Trial Lawyers' New Merger Tax*[1], and the problem was highlighted at our Legal Reform Summit that same year. As you know, several members of Delaware's distinguished Court of Chancery have expressed concern about this problem in recent years. There is good reason for that broad agreement—the data demonstrate that our country's M&A litigation system is broken:

[1] *See* Andrew Pincus, *The Trial Lawyers' New Merger Tax* (Oct. 2012), available at http://www.instituteforlegalreform.com/uploads/sites/1/M_and_A.pdf.

- For the past four years (2011-2014), 93% of all transactions valued over $100 million have been challenged by one or more lawsuits[2]—can anyone seriously believe that every such deal violates the law, and that things have gotten so much worse since 2005, when only 39% of such deals triggered a lawsuit?[3]

- These cases virtually never result in a judgment on the merits, relatively few are dismissed, and an overwhelming number (70% or more) settle.[4]

- Most settlements—79% over the past four years—require only additional disclosures; just 6% produce additional compensation for shareholders (the rest involved other changes to deal terms, such as a reduced termination fee)[5]; ten years ago more than half resulted in a monetary benefit and only 10% were disclosure only.[6]

- Although shareholders typically get nothing, the lawyers who file these cases do well: an average fee award *for disclosure-only settlements* of more than $465,000 in Delaware's Court of Chancery (and nearly $100,000 more in other jurisdictions).[7] That is a substantial amount of money for cases that produce very little, if anything, in the way of benefit for shareholders.

It is important to keep in mind, moreover, that this data does not quantify the burden that abusive lawsuits impose on innocent shareholders—in terms of defense costs, diversion of management time and attention, and deals not pursued because the total "merger tax" made them uneconomic.

More recently, attention has been focused on another element of abuse—the use of "professional plaintiffs" to file these actions. A study conducted by three law professors found that

> repeat plaintiffs are common because states typically do not limit the number of lawsuits that individual plaintiffs are allowed to file. As a result, law firms can use the same individuals time and again as plaintiffs in their lawsuits. Some individuals have filed 30, 40, or even 50 shareholder lawsuits over the past several years. Other plaintiffs' lawyers have themselves served as repeat plaintiffs or named close family members as plaintiffs.

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[2] *Shareholder Litigation Involving Acquisitions of Public Companies: Review of 2014 M&A Litigation* at 1 (2015), available at https://www.cornerstone.com/GetAttachment-/897c61ef-bfde-46e6-a2b8-5f94906c6ee2/Shareholder-Litigation-Involving-Acquisitions-2014-Review.pdf.

[3] *The Trial Lawyers' New Merger Tax*, *supra*, at 2.

[4] *Shareholder Litigation Involving Acquisitions of Public Companies*, *supra*, at 4.

[5] *Id.* at 5.

[6] *The Trial Lawyers' New Merger Tax*, *supra*, at 5.

[7] Robert M. Daines & Olga Koumrian, *Shareholder Litigation Involving Mergers and Acquisitions: Review of 2013 M&A Litigation* at 2, available at http://www.cornerstone.com/GetAttachment/7bd80347-124b-4b69-add5-575e33c3f61b/Settlements-of-M-and-A-Shareholder-Litigation.pdf.

> In a time when nearly all large mergers and acquisitions are challenged in court, the legal system needs shareholder plaintiffs who are ready and willing to protect absent class members from frivolous lawsuits. . . . [R]epeat plaintiffs with interests that separate them from the rest of the class are often unable to perform this crucial role.[8]

A recent Reuters investigative report concerned one plaintiff who has filed forty such claims, and never obtained a monetary benefit for shareholders.[9]

This problem, of course, is not a new one. It is one of the abuses of federal securities class actions addressed by the Private Securities Litigation Reform Act. The Senate Report on that legislation explained how this phenomenon contributes to the filing of abusive claims: "The proliferation of 'professional' plaintiffs has made it particularly easy for lawyers to find individuals willing to play the role of wronged investor for purposes of filing a class action lawsuit. Professional plaintiffs often are motivated by the payment of a 'bonus' far in excess of their share of any recovery."[10] As a result, the litigation is controlled by lawyers, and not by a client whose desire to redress an injury led to the filing of the lawsuit.

On the positive side, forum-selection bylaws appear to be addressing yet another form of abuse in M&A lawsuits—the filing of multiple lawsuits in multiple states challenging the same transaction, which forces the company (and therefore the innocent shareholders) to agree to payments to multiple plaintiffs' attorneys in order to resolve the litigation.[11] A survey of 2014 data found that 60% of deals were challenged in only one jurisdiction, compared to past years when that was true of only 40%.[12]

Of course, adoption of these bylaws will mean that—given Delaware's preeminence as a corporate domicile—more of these cases will be filed in Delaware, and only in Delaware. It is therefore critical that Delaware address the problem of abusive lawsuits, by ensuring that either corporations or the Court of Chancery have the tools they need to deter the filing of such claims while preserving the ability to file legitimate claims. After all, innocent shareholders will not benefit if the effect of Delaware Bar's proposal is to centralize all lawsuits in Delaware without eliminating abuse.

Some Delaware Bar members have expressed the view that the Court of Chancery has all of the authority it needs to deter abusive filings. Respectfully, the facts do not confirm that view: Delaware has not been immune from the epidemic of abuse in this area. And the claim that the

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[8] Stephen Choi, Jessica Erickson & Adam Pritchard, *Frequent Filers: The Problem of Shareholder Lawsuits and the Path to Reform* (March 2014), available at http://www.instituteforlegalreform.com-/uploads/sites/1/Frequent_Filers_Final_Version.pdf).

[9] Thomas Hals, *A TV stock picker's other life: leading an onslaught of class action suits*, Reuters (Feb. 18, 2015), available at http://www.reuters.com/investigates/special-report/lawsuit-class-kramer/.

[10] S. Rep. 104-98, 104th Cong., 1st Sess. 10 (1994).

[11] *See The Trial Lawyers' New Merger Tax*, *supra*, at 6-7.

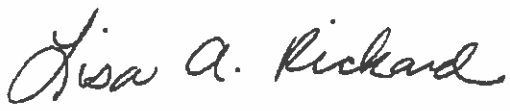
[12] *Shareholder Litigation Involving Acquisitions of Public Companies*, *supra*, at 3.

Court of Chancery will be able to use its authority to approve fee awards to deter abusive filings (by, for example, reducing fees for disclosure-only settlements) misunderstands the dynamic nature of litigation systems and the entrepreneurial acuity of plaintiffs' lawyers—something that we at ILR have observed in multiple contexts. Faced with reduced fees for such settlements, plaintiffs' lawyers are just as likely (perhaps more likely) to raise the price of settlement and thereby inflict even more cost on innocent shareholders.

What is needed are solutions—either in terms of bylaw authorization or additional tools for the Court of Chancery—that eliminate the incentives to file meritless lawsuits in the first place, and that address some of the more flagrant abuses such as the use of professional plaintiffs. Limiting corporations' authority to adopt fee-shifting bylaws, and thereby depriving them of the ability to protect shareholders against the costs of these claims, without at the same time providing such solutions is unjustified and unwise and entirely inconsistent with Delaware's tradition of a fair, clear legal framework.

Thank you for considering these views. I would be happy to discuss these important matters further with your and your colleagues.

Sincerely,



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