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Delaware Supreme Court Finds Fee-Shifting Bylaws Permissible

In an opinion that may dramatically change the landscape of stockholder litigation, the Delaware Supreme Court upheld in *ATP Tour, Inc. v. Deutscher Tennis Bund* a fee-shifting bylaw that required plaintiffs to bear the costs of intra-corporate litigation if the plaintiffs were not successful on the merits or did not achieve “in substance and amount, the full remedy sought.”

In finding that the bylaw was permissible as a matter of law, the court held that “[n]either the DGCL nor any other Delaware statute forbids the enactment of fee-shifting bylaws” and “[m]oreover, no principle of common law prohibits directors from enacting fee-shifting bylaws.” This conclusion follows from the fact that bylaws are a form of contract and that fee-shifting is a well-settled contractual device for allocating risk. The court notes that the adoption and application of such a fee-shifting bylaw must comply with a board’s fiduciary duties, but if the board so complies, such bylaws are facially permissible and enforceable, even for the purpose of deterring litigation. As the court holds, “[f]ee-shifting provisions, by their nature, deter litigation. Because fee-shifting provisions are not per se invalid, an intent to deter litigation would not necessarily render the bylaw unenforceable in equity.”

The opinion addresses a bylaw put in place in the context of a non-stock corporation, but the holding may be read to apply to all Delaware corporations. Whether such a bylaw is appropriate for a particular corporation, will, however, depend on a number of factors specific to such corporation and care should be taken in connection with an adoption of such a bylaw. Because this is the first case addressing fee-shifting bylaws, the reaction of proxy advisory firms and other interested parties in the corporate governance arena is yet to be known. Further, the court was careful to note that such a bylaw may be facially valid, but nevertheless be invalid if adopted or used for an inequitable purpose.

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This memorandum is not intended to provide legal advice, and no legal or business decision should be based on its content. Questions concerning issues addressed in this memorandum should be directed to:

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