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ATP Tour, Inc. v. Deutscher Tennis Bund

Delaware Supreme Court Rules that Fee-Shifting Provisions in Non-Stock Corporation Bylaws Are Facially Valid Under Delaware Law

In a recent [opinion](#), a unanimous Delaware Supreme Court sitting *en banc* upheld as a matter of law fee-shifting provisions in a non-stock corporation's bylaws requiring that plaintiffs bear the full costs of intra-corporate litigation if they do not obtain a judgment on the merits that substantially achieves, in substance and amount, the full remedy sought. In so finding, the Court ruled that nothing in the DGCL prohibits the adoption of fee-shifting bylaws and further indicated that by allocating intra-corporate litigation risk such provisions also satisfy Section 109(b) of the DGCL requiring that bylaws relate to the "business of the corporation, the conduct of its affairs, and its rights or powers or the rights or powers of its stockholders, directors, officers or employees".¹ In the Court's view, fee-shifting bylaws also are not prohibited under Delaware common law since corporate bylaws are contracts among shareholders, and contracting parties can agree to modify Delaware's general rule that litigants pay their own attorneys' fees and costs by requiring that an unsuccessful litigant reimburse the other's fees.

However, the Court made clear that the fact that a bylaw is facially valid does not mean that it is enforceable, citing to a number of cases in which the Delaware courts have found bylaws not to be enforceable because they were adopted or used for an inequitable purpose. The Court observed that the enforceability of a fee-shifting bylaw will turn on "the manner in which it was adopted and the circumstances under which it was invoked", but indicated that a board's intention to deter litigation from its members "is not invariably an improper purpose".² According to the Court, although "[f]ee shifting provisions, by their nature, deter litigation", they are not per se invalid.³

Because the *ATP Tour* opinion was rendered in the context of questions of law certified to the Court by the Delaware federal district court, the decision did not directly address the enforceability of the bylaw at issue – a fee-shifting provision unilaterally adopted by the board of a Delaware non-stock membership

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corporation after the plaintiffs joined the corporation but before the board's actions giving rise to the fiduciary duty and antitrust claims. In addition, citing *Boilermakers Local 154 Retirement Fund v. Chevron Corp.*,⁴ the Court ruled that an otherwise valid fee-shifting bylaw may be enforced against members who join a corporation before the bylaw's unilateral enactment by the board so long as the charter authorizes the directors to adopt bylaws.

While the *ATP Tour* opinion was decided based on DGCL and Delaware common law principles applicable to both Delaware stock and non-stock corporations, it leaves unanswered whether stock corporation boards may rely on the decision to support their unilateral enactment of fee-shifting bylaws. To the extent it does apply to stock corporations, directors who are authorized by the charter to adopt bylaws would have a path for combatting certain shareholder litigation, subject to judicial review of the circumstances of the bylaws' use in any particular litigation. Directors should also keep in mind, however, that it is unclear what reaction the adoption of such a bylaw would draw from investors and proxy advisory firms, who generally react negatively to the unilateral adoption by a board of bylaws they view as limiting shareholder rights.⁵

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ENDNOTES

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- ¹ The Court noted that a company's charter may explicitly or implicitly by silence permit fee-shifting bylaws.
- ² *ATP Tour, Inc. v. Deutscher Tennis Bund*, No. 534, 2013, slip op. at 10, 13 (Del. May 8, 2014).
- ³ *Id.* at 13.
- ⁴ 73 A.3d 934 (Del. Ch. 2013) (holding that forum selection bylaws are valid and presumptively enforceable under Delaware law). For a full discussion of then Chancellor (now Delaware Supreme Court Chief Justice) Strine's *Chevron* decision, see our publication, dated June 28, 2013, entitled "[Delaware Ruling on Exclusive Forum Bylaws](#)".
- ⁵ For example, Glass-Lewis will generally recommend a withhold vote against the chair of the governance committee if a company unilaterally adopts an exclusive forum bylaw, and Institutional Shareholder Services generally opposes such bylaws unless the company can show that it has been materially harmed by shareholder litigation outside its jurisdiction of incorporation. In addition, ISS has recommended withhold votes against directors where the board unilaterally adopted bylaws that restrict directors from receiving third-party compensation. See our publication, dated January 30, 2014, entitled "[2014 Proxy Season Developments](#)", for a discussion of ISS's policies and recommendations on the topic.

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