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Delaware's Balancing Act

Law Working Paper N° 167/2010
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John Armour
University of Oxford and ECGI
Bernard Black
Northwestern University and ECGI
Brian Cheffins
Cambridge University and ECGI

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ECGI Working Paper Series in Law

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Abstract

Delaware's courts and well-developed case law are widely seen as integral elements of Delaware's success in attracting incorporations. However, as we show using empirical evidence involving reported judicial decisions and filed cases concerning large mergers and acquisitions, leveraged buyouts, and options backdating, Delaware's popularity as a venue for corporate litigation has dropped sharply. Today, a majority of shareholder suits involving Delaware companies are being brought and decided elsewhere. We examine in this Article the implications of this "out-of-Delaware" trend, emphasizing a difficult balancing act that Delaware faces. If Delaware accommodates litigation too readily, companies, fearful of lawsuits, may incorporate elsewhere. But if plaintiffs' attorneys find the Delaware courts unwelcoming, they can often file cases in other courts. Delaware could risk losing its status as the de facto national corporate law court, as well as the case flow that lets it provide the rich body of precedent that is part of Delaware's overall corporate law "brand." We assess how the Delaware courts and legislature, and Delaware companies, might respond to this threat to Delaware's pre-eminence as the leading forum for corporate cases, as well as incorporations.

Keywords: Delaware courts, corporate litigation, forum shopping

JEL Classifications: K22, K41

John Armour
Hogan Lovells Professor of Law and Finance
University of Oxford, Faculty of Law
St Cross Building, St Cross Road
Oxford OX1 3UL, United Kingdom
e-mail: john.armour@law.ox.ac.uk

Bernard Black
Nicholas J. Chabraja Professor
Northwestern University, Law School and Kellogg School of Management
375 East Chicago Avenue
Chicago, Illinois 60611, United States
e-mail: bblack@northwestern.edu

Brian Cheffins*
S.J. Berwin Professor of Corporate Law
Cambridge University, Faculty of Law
10 West Road
Cambridge CB3 9DZ, United Kingdom
phone: +44 1223 330084
e-mail: brc21@cam.ac.uk

*Corresponding Author

Delaware's Balancing Act

JOHN ARMOUR, BERNARD BLACK AND BRIAN CHEFFINS*

Delaware's courts and well-developed case law are widely seen as integral elements of Delaware's success in attracting incorporations. However, as we show using empirical evidence involving reported judicial decisions and filed cases concerning large mergers and acquisitions, leveraged buyouts, and options backdating, Delaware's popularity as a venue for corporate litigation is under threat. Today, a majority of shareholder suits involving Delaware companies are being brought and decided elsewhere. We examine in this Article the implications of this "out-of-Delaware" trend, emphasizing a difficult balancing act that Delaware faces. If Delaware accommodates litigation too readily, companies, fearful of lawsuits, may incorporate elsewhere. But if plaintiffs' attorneys find the Delaware courts unwelcoming, they can often file cases in other courts. Delaware could risk losing its status as the de facto national corporate law court, as well as the case flow that lets it provide the rich body of precedent that is part of Delaware's overall corporate law "brand." We assess how the Delaware courts and legislature, and Delaware companies, might respond to this threat to Delaware's pre-eminence as the leading forum for corporate cases, as well as incorporations.

I. INTRODUCTION 1346
II. THE NATURE AND EXTENT OF THE OUT-OF-DELAWARE TREND 1351
A. THE JURISDICTIONAL TERRAIN 1351
B. EMPIRICAL EVIDENCE 1353
C. ANECDOTAL EVIDENCE 1363
III. WHAT HAS PROMPTED THE OUT-OF-DELAWARE TREND? 1364
A. WHO DECIDES WHERE LAWSUITS ARE BROUGHT? 1364

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* Armour is Hogan Lovells Professor of Law and Finance, Faculty of Law, University of Oxford, e-mail: john.armour@law.ox.ac.uk. Black is Nicholas J. Chabraja Professor at Northwestern University, Law School and Kellogg School of Management, e-mail: bblack@northwestern.edu. Cheffins is S.J. Berwin Professor of Corporate Law, Faculty of Law, Cambridge University, e-mail: brc21@cam.ac.uk. We thank Nathan Chuang, Mitch Fagen, Jonell Goco, Patrick Luff, Jose Miguel Mendoza, Ji Min Park, Alex Ruge, and Li Weng for excellent research assistance, and Columbia Law School, the Searle Center on Law, Regulation, and Economic Growth at Northwestern Law School, the University of Oxford Law Faculty, and University of Texas Law School for financial support. We are grateful for comments on this Article, and a companion empirical paper, by Keith Bishop, Jill Fisch, Jeff Gordon, and Delaware Vice-Chancellor Travis Laster, and feedback at the American Law and Economics Association (2011 annual meeting), Canadian Law and Economics Association (2010 annual meeting), Conference on Empirical Legal Studies (2010), Harvard Law School, Stanford Law School, University of Illinois Law School, University of Leeds Law School, University of San Diego Law School, USD Law Center for Corporate and Securities Law, Vanderbilt Law School Conference on Corporate Law (2010), and Columbia Law School Conference on The Delaware Court of Chancery: Change and Continuity (2011). We have also benefitted from discussions with various corporate lawyers, including Randall Baron, Peter Carter, Travis Downs, Joel Friedlander, Stuart Grant, William Lafferty, Mark Lebovitch, Roger Magnuson, Ted Mirvis, Stephen Radin, and Bryn Valler.

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B. PREDICTABILITY, PRO-DEFENDANT BIAS, AND THE TIME DIMENSION .. 1365
C. JUDICIAL ATTITUDES CONCERNING THE PLAINTIFFS' BAR 1367
D. ATTORNEYS' FEES 1370
E. SELECTION OF LEAD COUNSEL 1372
IV. THE DELAWARE COURTS' BALANCING ACT 1380
A. JUDICIAL INCENTIVES TO REVERSE THE OUT-OF-DELAWARE TREND ... 1381
B. STEPS DELAWARE JUDGES COULD TAKE TO REVERSE THE OUT-OF-DELAWARE TREND 1384
C. WILL THE DELAWARE COURTS SEEK TO REGAIN MARKET SHARE? 1387
V. OTHER POTENTIAL RESPONSES TO THE OUT-OF-DELAWARE TREND 1392
A. SELF-HELP BY DELAWARE COMPANIES 1392
B. DELAWARE LEGISLATION 1394
C. FEDERAL REFORM 1395
VI. THE PROS AND CONS OF THE OUT-OF-DELAWARE TREND 1396
A. THE MIXED IMPLICATIONS OF FORUM SHOPPING 1396
B. QUALITY OF JUDICIAL DECISION-MAKING 1397
C. IMPACT ON THE DELAWARE BRAND 1398
VII. CONCLUSION 1398
REFERENCES 1400

I. INTRODUCTION

"I'm a litigator—and there's only one rule in litigation: Three things matter—location, location, location."[1]

A core feature of U.S. corporate law is regulatory competition. Companies can choose which state's corporate law will govern their affairs and states vie—to some extent—to attract companies to incorporate. There has been intense scholarly debate as to whether this competition for incorporations, which Delaware dominates, is—for good or ill—a "race to the bottom" or a "race to the top."[2] In this Article we focus on a different aspect of corporate federalism that has received little academic attention but has important implications: where are shareholder lawsuits involving Delaware companies actually filed and resolved?

The answer has traditionally been, "Delaware, of course." The Delaware courts, termed "the Mother Court[s] of corporate law,"[3] have decided most major corporate

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1. *Anywhere but Chancery: Ted Mirvis Sounds an Alarm and Suggests Some Solutions*, 7 M&A J. 17, 18 (2007) (quoting Ted Mirvis of Wachtell, Lipton, Rosen and Katz).

2. The "race to the bottom" terminology was first coined by William L. Cary, *Federalism and Corporate Law: Reflections upon Delaware*, 83 YALE L.J. 663, 666 (1974). Ralph Winter saw instead a "race to the top": Ralph Winter, *Private Goals and Competition Among State Legal Systems*, 6 HARV. J.L. & PUB. POL'Y 127, 128–29 (1982). For more recent assessments, see, for example, Jill E. Fisch, *The Peculiar Role of the De1aware Courts in the Competition for Corporate Charters*, 68 U. CIN. L. REV. 1061 (2000); Lawrence A. Hamermesh, *The Policy Foundations of Delaware Corporate Law*, 106 COLUM. L. REV. 1749 (2006); Lucian Arye Bebchuk & Assaf Hamdani, *Vigorous Race or Leisurely Walk: Reconsidering the Competition over Corporate Charters*, 112 YALE L.J. 553 (2002).

3. Kamen v. Kemper Fin. Servs., Inc., 908 F.2d 1338, 1343 (7th Cir. 1990), *rev'd on*

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law cases in the United States, and courts in other states have often applied Delaware precedents to non-Delaware corporations. An extensive body of precedent, developed by expert judges, has been a key part of Delaware's "value-added" for firms, which has helped to sustain its high share in the market for corporate law, despite premium pricing in the form of sizeable "franchise taxes" levied on firms that incorporate there.[4] But, as we show in a companion paper, Delaware's share of shareholder suits against directors has dropped sharply over the last 15 years.[5] Some plaintiffs' law firms now prefer to file these suits "anywhere *but*" Delaware.[6] Some companies are responding by adopting bylaws or charter provisions specifying that claims arising under Delaware corporate law should be brought in Delaware.[7] A 2011 California case held that such a "forum selection" bylaw is unenforceable,[8] but more battles over forum selection clauses can be expected.

In exploring the "market" for corporate lawsuits, we provide a novel twist on the well-known debate over the competition for corporate charters.[9] The out-of-Delaware trend implicates a different form of corporate law competition scarcely noticed until recently, namely the venue where suits are filed.[10] This

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other grounds, 500 U.S. 90 (1991), *quoted in* Jerue v. Millett, 66 P.3d 736, 745, n.26 (Alaska 2003); Stephen A. Radin, *The New Stage of Corporate Governance Litigation: Section 220 Demands—Reprise*, 28 CARDOZO L. REV. 1287, 1287–88 (2006).

4. On Delaware's premium pricing, see Marcel Kahan & Ehud Kamar, *Price Discrimination in the Market for Corporate Law*, 86 CORNELL L. REV. 1205, 1210–11 (2001).

5. John Armour, Bernard S. Black & Brian R. Cheffins, *Is Delaware Losing Its Cases?* 9 J. EMPIRICAL LEGAL STUD. (forthcoming 2012) [hereinafter *ABC Losing Cases*], *available at* http://ssrn.com/abstract=1578404.

6. As in the phrase used by Ted Mirvis. *See Anywhere but Chancery* (2007), *supra* note 1, at 18 (emphasis added).

7. Joseph A. Grundfest, *Choice of Forum Provisions in Intra-Corporate Litigation: Mandatory and Elective Approaches (The 2010 Pileggi Lecture)* (Rock Center for Corporate Governance at Stanford University Working Paper No. 91, 2010), *available at* http://ssrn.com/abstract=1690561.

8. Galaviz v. Berg., 763 F. Supp. 2d 1170 (N.D. Cal. Jan. 3, 2011) (involving an Oracle Corp. bylaw).

9. *See generally* Kagan Kocaoglu, A Comparative Bibliography: Regulatory Competition on Corporate Law (Mar. 2008) (unpublished working paper), *available at* http://ssrn.com/abstract=1103644.

10. For other recent papers addressing aspects of forum competition, see Jessica Erickson, *Corporate Governance in the Courtroom: An Empirical Analysis*, 51 WM. & MARY L. REV. 1749 (2010) (finding that derivative lawsuits are commonly filed in federal court); Jennifer J. Johnson, *Securities Class Actions in State Court*, 80 U. CIN. L. REV. (forthcoming 2012), *available at* http://ssrn.com/abstract=1856695; Sara Lewis, *Transforming the "Anywhere but Chancery" Problem into the "Nowhere but Chancery" Solution*, 14 STAN. J.L. BUS. & FIN. 199 (2008); Edward B. Micheletti & Jenness E. Parker, *Multi-Jurisdictional Litigation: Who Caused This Problem, and Can it be Fixed?*, 37 DEL. J. CORP. L. 1 (2012); Brian JM Quinn, *Shareholder Lawsuits, Status Quo Bias, and Adoption of the Exclusive Forum Provision*, 45 U.C. DAVIS L. REV. 137, 155–56 (2011); Faith Stevelman, *Regulatory Competition, Choice of Forum, and Delaware's Stake in Corporate Law*, 34 DEL. J. CORP. L. 57 (2009); Matthew D. Cain & Steven M. Davidoff, A Great Game: The Dynamics of State Competition and Litigation (Apr. 1, 2012) (unpublished manuscript),

Electronic copy available at: http://ssrn.com/abstract=1677400

Article is the first to address systematically the issues the out-of-Delaware trend poses for litigants, judges, and legislators.

To set the scene, we summarize our empirical data confirming the trend. We then explore why the trend has arisen and consider its implications for Delaware's dominance as a locus for incorporations and as the principal source of corporate case law. We also examine how the Delaware courts, its legislature, and companies incorporated there might respond.

The out-of-Delaware trend highlights a difficult balancing act faced by Delaware, especially its judiciary. If Delaware accommodates shareholder suits too readily, plaintiffs' attorneys will file an excess of cases, and companies, fearful of litigation, may incorporate in a different state. On the other hand, if plaintiffs' attorneys believe Delaware courts are unwelcoming, they may launch their actions elsewhere. Some of these cases will present opportunities to develop new precedents which will be missed by Delaware courts, thus compromising Delaware's responsiveness to new events. A pronounced out-of-Delaware trend could also mean Delaware judges will forfeit some of their current national recognition and esteem, and Delaware-based lawyers will lose status and income. Recent efforts by the Delaware courts to discourage the filing of "weak" cases illustrate the difficulty of this balancing act, as taking these steps may have exacerbated the out-of-Delaware trend. Moreover, a strong effort to recapture litigation "market share" could discredit the Delaware judiciary or prompt further federalization of corporate law.[11]

While views differ on the merits of state competition for incorporations of publicly traded companies, there is little doubt that Delaware is the big winner. More than 80% of public companies that incorporate outside their headquarters state select Delaware, and about 60% of all U.S. public companies are incorporated there.[12] Mark Roe has gone so far as to speculate that Delaware corporate law could be "too big to fail,"[13] and Chancellor Leo Strine of Delaware's Court of Chancery has acknowledged that the state could be perceived as "a bit of a fat and happy monopolist."[14]

Various explanations have been given for Delaware's dominance. The state's small size and heavy reliance on revenues from franchise taxes reputedly combine to yield a credible commitment to be responsive to corporate need.[15] There are network externalities associated with choosing Delaware law, in the form of a well-developed infrastructure of professionals supplying incorporation and legal

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available at http://ssrn.com/abstract=1984758.

11. Marcel Kahan & Edward Rock, *Symbiotic Federalism and the Structure of Corporate Law*, 58 VAND. L. REV. 1573 (2005); Mark J. Roe, *Delaware's Competition*, 117 HARV. L. REV. 588 (2003).

12. Bebchuk & Hamdani (2002), *supra* note 2, at 567 tbl.2, 578 tbl.5.

13. Mark J. Roe, *Is Delaware's Corporate Law Too Big to Fail?*, 74 BROOK. L. REV. 75 (2008).

14. Leo E. Strine, Jr., *Delaware's Corporate-Law System: Is Corporate America Buying an Exquisite Jewel or a Diamond in the Rough? A Response to Kahan & Kamar's* Price Discrimination in the Market for Corporate Law, 86 CORNELL L. REV. 1257, 1265 (2001). Strine was appointed Chancellor in 2011, after twelve years as a Vice-Chancellor.

15. Hamermesh (2006), *supra* note 2, at 1753–54; ROBERTA ROMANO, THE GENIUS OF AMERICAN CORPORATE LAW 38, 44 (1993).

services.[16] Finally, and crucially for our purposes, the court system is a key aspect of the Delaware "brand."[17] For those who see Delaware as winning a "race to the bottom," Delaware judges ensure that the state offers "manager-friendly" decisions to accompany its manager-friendly statute.[18] For those who take the view that Delaware's dominance of corporate law reflects a "race to the top" toward efficient corporate law, Delaware-incorporated firms benefit from extensive precedents and the decision-making expertise of the Delaware judges.[19]

Delaware's corporate law delegates regulatory power liberally to its judges, often favoring flexible, judicially adopted standards. Consequently, much of what matters in Delaware corporate law is a judicial construct, including the fiduciary duties of directors, officers, and controlling shareholders, and the prerequisites for bringing a derivative suit.[20] Thus, the depth and clarity of Delaware corporate law could be compromised if case flow were to shrink.[21] Delaware judges are aware of this. As Chancellor Strine stated in a 2007 case: "The important coherence-generating benefits created by our judiciary's handling of corporate disputes are endangered if our state's compelling public policy interest in deciding these disputes is not recognized . . . ."[22] Chancellor Strine's colleague, Vice Chancellor Travis Laster, was sufficiently concerned about litigation migrating out of his state to issue a general invitation to firms in a 2010 opinion to adopt charter provisions making Delaware the exclusive forum for corporate suits.[23]

One might think there would be little risk of the Delaware courts losing their case flow. In 2010 the U.S. Chamber of Commerce's Institute for Legal Reform ranked Delaware first among the 50 states for the quality and fairness of its litigation environment for the eighth year in a row.[24] Jonathan Macey and Geoffrey

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16. Michael Klausner, *Corporations, Corporate Law, and Networks of Contracts*, 81 VA. L. REV. 757, 846 (1995).

17. On the idea that Delaware's legal regime is a "brand," with the judiciary as a key element, see Omari Scott Simmons, *Branding the Small Wonder: Delaware's Dominance and the Market for Corporate Law*, 42 U. RICH. L. REV. 1129 (2008).

18. *See, e.g.*, Cary (1974), *supra* note 2, at 670, 672 ("[J]udicial decisions can best be reconciled on the basis of a desire to foster incorporation in Delaware. . . . Delaware corporate decisions lean . . . to minimal standards of director responsibility . . . .").

19. Bernard S. Black, *Is Corporate Law Trivial?: A Political and Economic Analysis*, 84 NW. U. L. REV. 542, 589–91 (1990); Robert Daines, *Does Delaware Law Improve Firm Value?*, 62 J. FIN. ECON. 525, 540 (2001); William H. Rehnquist, *The Prominence of the Delaware Court of Chancery in the State-Federal Joint Venture of Providing Justice*, 48 BUS. LAW. 351, 354 (1992).

20. Kahan & Rock (2005), *supra* note 11, 1591–92; Hamermesh (2006), *supra* note 2, 1777–78.

21. Stevelman (2009), *supra* note 10, at 122.

22. *In re* The Topps Co. S'holders Litig., 924 A.2d 951, 959 (Del. Ch. 2007).

23. *In re* Revlon, Inc. S'holders Litig., 990 A.2d 940 (Del. Ch. 2010).

24. U.S. CHAMBER INSTITUTE FOR LEGAL REFORM, 2010 CHAMBER OF COMMERCE STATE LIABILITY SYSTEMS RANKING STUDY 14 (2010), http://court.state.de.us/Superior/pdf/harris_2010.pdf; *see also* Scott A. Holt, *Delaware Courts Ranked 1st by U.S. Chamber of Commerce*, DEL. EMP. L. BLOG (Apr. 24, 2008), http://www.delawareemploymentlawblog.com/2008/04/delaware_courts_ranked_1st_by.html; Brett Melson, *Delaware Is #1*, HARV. BUS. SERV. BLOG (June 3, 2009), http://blog.delawareinc.com/tag/us-chamber-of-

Miller even argued in a widely cited 1987 article that, due to capture of the litigation process by local lawyers, Delaware is unduly litigation friendly.[25]

It cannot be taken for granted, however, that corporate litigation will be launched in Delaware courts. Plaintiffs' attorneys usually have a choice of venue when filing a corporate suit. If they perceive that filing outside Delaware is advantageous, they may well do so. They might avoid Delaware because they believe its judges tend to favor corporate defendants. Delaware's high rank from the Chamber of Commerce may be exactly what plaintiffs do not want. Plaintiffs' attorneys could also react to what the Delaware judiciary thinks of *them* and how it polices the fees they are awarded when a case settles or the plaintiffs prevail at trial. Over the last decade, Delaware judges have criticized plaintiffs' attorneys who have brought weak cases, sometimes sharply. Delaware judges have also denounced lawyers racing to file first to gain strategic advantage[26] and have sometimes cut back attorney fee requests when cases settle, including requests the defendants have agreed not to oppose.

The cases Delaware loses because plaintiffs' attorneys file lawsuits elsewhere could well include "good" cases, which the state's courts need to develop new precedents. A recent wave of "option backdating" suits illustrates the point. Many of these cases were widely viewed as meritorious, and a fair number generated settlements of $10 million or more. Nevertheless, our research shows that the vast majority of option backdating suits involving Delaware companies were filed outside Delaware. The Delaware courts thus missed an opportunity to address the responsibility of directors to oversee option granting practices.

The loss of potentially important cases appears to generalize beyond options backdating. For example, in our empirical research, we also studied cases that give rise to publicly distributed opinions—the ones that generate precedents. Delaware is losing market share for these cases as well.

Delaware's loss of litigation market share prompts a series of questions. What has caused this trend? If Delaware companies want the Delaware courts to decide their corporate law disputes, how can they make this more likely? If the Delaware courts or legislature want Delaware to recapture litigation market share, how might this be achieved? By how much will the migration of corporate suits away from Delaware courts weaken the Delaware brand? And is the out-of-Delaware trend to be welcomed?

We address these questions below, drawing on our empirical research and on a series of interviews with plaintiffs' and defense counsel. On the plaintiffs' side, we spoke to lawyers who approach Delaware from a variety of perspectives. Some prefer to file in Delaware. Others avoid Delaware. Still others make a case-by-case judgment call. With defense counsel, we sought to gauge awareness of the out-of-Delaware trend, to learn what responses the trend has elicited, and to find out what responses they expect from companies and the defense bar.

The Article proceeds as follows. Part II provides an overview of the jurisdictional terrain and summarizes our empirical evidence on the

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commerce/.

25. Jonathan R. Macey & Geoffrey P. Miller, *Toward an Interest-Group Theory of Delaware Corporate Law*, 65 TEX. L. REV. 469 (1987).

26. *See, e.g.*, King v. VeriFone Holdings, Inc., 994 A.2d 354, 357 (Del. Ch. 2010) (Chancellor Strine criticized the "lead counsel Olympics race.").

out-of-Delaware trend. Part III explores why Delaware has been losing its cases. Part IV focuses on the difficult balancing act that the out-of-Delaware trend calls upon Delaware's judges to perform. Part V discusses potential responses by firms and legislators to the migration of cases away from Delaware. Part VI assesses the normative implications of the out-of-Delaware trend. Part VII concludes.

II. THE NATURE AND EXTENT OF THE OUT-OF-DELAWARE TREND

A. The Jurisdictional Terrain

It is conventional wisdom that most corporate law cases involving Delaware public companies flow to Delaware.[27] William Cary, when he famously characterized Delaware as the winner in a race to the bottom for incorporation business, remarked on "the relative ease of entry into Delaware courts for suits against corporate directors."[28] Roberta Romano, a "race to the top" advocate, reported that "most Delaware firms are in fact sued in Delaware."[29] The pre-eminent status of Delaware courts has strong historical roots. Norman Veasey, a former chief justice of the Delaware Supreme Court, has observed that the flow of corporate cases to Delaware extends back at least to the 1950s.[30]

Delaware incorporation typically ensures that Delaware's substantive law will control in a suit under corporate law and that such a suit can be brought in Delaware.[31] However, suits under corporate law can also be filed in any other court with both subject matter jurisdiction over the claim and personal jurisdiction over the defendants. In practice, the courts of a company's headquarters state are almost always an available forum for both direct suits (including class actions) and derivative suits. Courts of general jurisdiction in that state will have subject matter jurisdiction, and personal jurisdiction over the directors and officers will normally be available as well.[32]

The federal courts in a Delaware company's headquarters state will also normally have personal jurisdiction over the directors and officers, and thus may offer a third potential forum. For subject matter jurisdiction, diversity jurisdiction is

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27. Douglas M. Branson, *Indeterminacy: The Final Ingredient in an Interest Group Analysis of Corporate Law*, 43 VAND. L. REV. 85, 91 (1990) (describing "the never ending flow of lawsuits to Delaware Chancery Court and appeals to the Delaware Supreme Court"); Ehud Kamar, *A Regulatory Competition Theory of Indeterminacy in Corporate Law*, 98 COLUM. L. REV. 1908, 1926 (1998); Macey & Miller (1987), *supra* note 25, at 496.

28. Cary (1974), *supra* note 2, at 686.

29. ROMANO (1993), *supra* note 15, at 41.

30. E. Norman Veasey, *Musings from the Center of the Corporate Universe*, 7 DEL. L. REV. 163, 164, 167 (2004).

31. Jack B. Jacobs, *The Reach of State Corporate Law Beyond State Borders: Reflections upon Federalism*, 84 N.Y.U. L. REV. 1149, 1159–60 (2009); Larry E. Ribstein & Erin Ann O'Hara, *Corporations and the Market for Law*, 2008 U. ILL. L. REV. 661, 662. Directors and officers must consent to personal jurisdiction in Delaware as a condition of incorporation. DEL. CODE ANN. tit. 10, § 3114(a)–(b) (2011).

32. Most companies hold at least some board meetings at their headquarters; this without more should provide the minimum contacts needed for personal jurisdiction.

usually available for derivative suits.[33] For direct suits, plaintiffs can sometimes combine a state law claim under corporate law with a related federal claim, often under securities law, and rely on "supplemental" (or "pendent") federal jurisdiction over the corporate law claim.[34]

Defendants in corporate litigation have some scope to challenge the litigation venue choices plaintiffs make. If suits involving similar facts have been filed both in Delaware and elsewhere, the defendants could seek a stay or dismissal of the non-Delaware proceedings on *forum non conveniens* grounds.[35] Defendants in practice may be reluctant to seek a stay because they "do not wish to alienate potential fact-finders by openly fleeing one court for another."[36] Moreover, success in state court on a *forum non conveniens* motion is not assured, with the likelihood of success decreasing if the case was filed first in that state court and there has been significant progress in the litigation.[37]

An alternative to a motion to dismiss a suit in one jurisdiction in favor of another jurisdiction is for the defendants to use a "one forum" motion. The defendants will apply to both forums for an order that the courts involved confer and determine where the case should proceed.[38] An obvious risk is that, if the orders are granted and the courts do confer, proceedings may not occur in the defendant's preferred forum.

For cases brought in federal courts under supplemental jurisdiction, a federal judge may, in the interests of comity and judicial efficiency, dismiss or stay a derivative lawsuit filed in federal court where a single state court action would serve the best interests of the corporation and its stockholders.[39] However, success

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33. Gilbert Newman, *Manufacturing Diversity Jurisdiction*, 14 VILL. L. REV. 727, 729 (1969).

34. Stanley A. Kaplan, *Fiduciary Responsibility in the Management of the Corporation*, 31 BUS. LAW. 883, 890 (1976); United Mine Workers v. Gibbs, 383 U.S. 715 (1966) (test for "pendent" jurisdiction now included in "supplemental jurisdiction"); Finley v. United States 490 U.S. 545 (1989). For class actions in general, Congress has introduced various reforms designed to expand federal court jurisdiction, primarily the Securities Litigation Uniform Standard Act of 1998, Pub. L. No. 105-353, 112 Stat. 3227 (codified in scattered sections of 15 U.S.C.), and the Class Action Fairness Act of 2005, Pub. L. No. 109-2, 119 Stat. 4 (codified at 28 U.S.C. § 1453 (2006)). *See* Howard M. Erichson, *CAFA's Impact on Class Action Lawyers*, 156 U. PA. L. REV. 1593, 1597, 1601 (2008). But these statutes both contain "Delaware carve-outs" and thus do not cover corporate law cases. *See* Kahan & Rock (2005), *supra* note 11, 1587–88; Lawrence A. Hamermesh, *Reputation of Delaware Courts Wins Carve-Out in U.S. House Bill Regulating Class Actions*, DEL. L. WKLY., Oct. 5, 1999, at 7.

35. Debra Lyn Bassett, *The Forum Game*, 84 N.C. L. REV. 333, 344, 353, 389 (2006); Note, *Forum Shopping Reconsidered*, 103 HARV. L. REV. 1677, 1679 (1990).

36. Brief of Special Counsel Gregory P. Williams, at 3, Scully v. Nighthawk Radiology Holdings, Inc., C.A. No. 5890–VCL (Del. Ch. Mar. 11, 2011).

37. Geoffrey P. Miller, *Overlapping Class Actions*, 71 N.Y.U. L. REV. 514, 522 (1996).

38. Micheletti & Parker (2012), *supra* note 10, at 18–19.

39. *See, e.g.*, Weiss v. Doyle, 178 F. Supp. 566 (S.D.N.Y. 1959). On the factors that influence stay decisions, see Jean F. Rydstrom, Annotation, *Stay of Action in Federal Court Until Determination of Similar Action Pending in State Court*, 5 A.L.R. FED. 10, §§ 5[a], 6[a] (1970).

on such a motion is not assured. Factors federal courts have cited when denying applications for a stay in shareholder litigation include the federal courts having diversity jurisdiction, the related state court case not having been significantly litigated, the parties not facing undue hardship to travel to litigate in federal court, and the federal complaint not being a "mirror image" of the state court complaint.[40]

B. Empirical Evidence

Until recently, little empirical research had been done on venue choice in corporate law, and none has been done with an explicit time trend.[41] Our data, described in more detail in a companion paper,[42] confirm the conventional wisdom on Delaware's popularity at the start of our study period (the mid-1990s), and its diminishing market share since then. We use four different datasets, and a combination of different strategies for identifying lawsuits, to document the out-of-Delaware trend, focusing in each instance on Delaware-incorporated public companies.

1. Reported Decisions

Our first dataset involves cases where a written decision is publicly available, either on a preliminary motion or after a trial. We collected all reported decisions from Westlaw, Lexis, and the Delaware Chancery Court website from 1995 to 2009 arising from lawsuits where directors of public corporations were named as defendants in claims brought under corporate law.[43] Given that a rich body of precedents is an oft-cited Delaware strength, this dataset provides direct evidence on the extent to which the out-of-Delaware trend puts this aspect of the Delaware brand under threat. Also, a judge is more likely to issue an opinion in cases that are vigorously contested and have implications for future litigants.[44] Thus, a written

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40. Tabas v. Mullane, 608 F. Supp. 759, 763 (D.N.J. 1985) (application for stay dismissed on the basis there was "no previously filed, significantly litigated, or more advanced state action"); Loeb v. Whittaker Corp., 333 F. Supp. 484, 489 (S.D.N.Y. 1971) ("mirror image"); La. Mun. Police Emps. Ret. Sys. v. Medco Health Solutions, Inc., C.A. No. 2:11-cv-4211(DMC)(MF), 2011 WL 4386774, at *4 (D.N.J. Sept. 19, 2011) (diversity jurisdiction; lack of litigation activity in state court).

41. Several studies of aspects of corporate venue choice have recently appeared in addition to our own. *See* Erickson (2010), *supra* note 10; Quinn (2011), *supra* note 10; Johnson (2012), *supra* note 10; Cain & Davidoff (2012), *supra* note 10. These studies generally confirm the out-of-Delaware trend we report but only cover the period after the out-of-Delaware trend was well underway. We discuss each below.

42. *ABC Losing Cases* (2012), *supra* note 5.

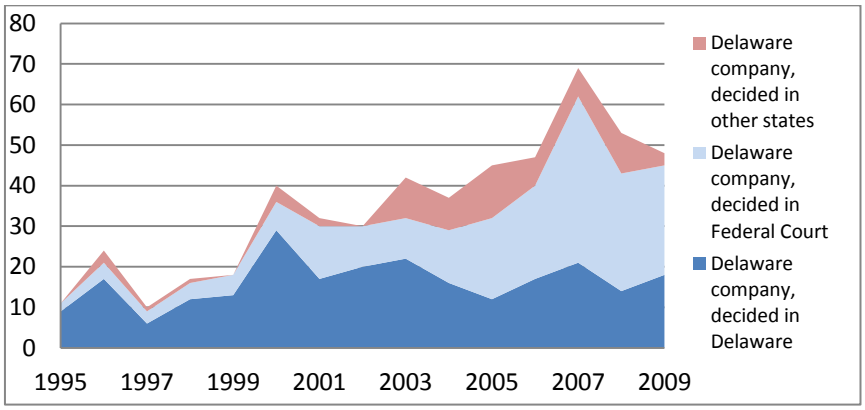
43. We searched for suits (1) arising under corporate law, (2) in which one or more directors was a defendant, and (3) that produced at least one publicly available judicial decision between 1995 and 2009. For Westlaw, we searched the Allcases library; for Lexis, we searched the Mega library. We also searched the Delaware Court of Chancery website, which contains all written judicial opinions by Chancery Court judges from 2000 on. If a case generated more than one decision, we assigned the case to the year of the first decision. For details on our search criteria, see *ABC Losing Cases* (2012), *supra* note 5.

44. RUGGERO J. ALDISERT, OPINION WRITING 19–20 (2d ed. 2009) (providing guidance

decision is a proxy, albeit a crude one, for case importance. This dataset accordingly provides evidence on the extent to which significant cases are migrating away from Delaware.

Our dataset includes 704 cases over 15 years, of which 540 (77%) involved Delaware companies. Figure 1 summarizes our results for these companies. The number of cases with decisions in Delaware remained fairly constant over time. In contrast, there was dramatic growth in the number of decisions outside Delaware, especially in the federal courts.

Figure 1: Lawsuits Against Delaware Companies with Written Decisions, 1995–2009

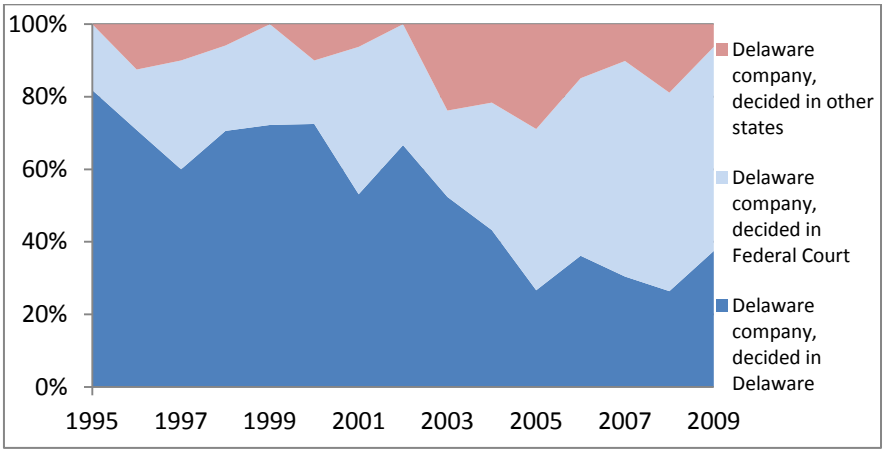


Number of cases involving suits under corporate law against directors of Delaware public companies and location of decision, for cases with one or more reported decisions on Westlaw, Lexis, or the Delaware Chancery Court website, with the first reported decision issued between 1995 and 2009.

Figure 2 converts this flow of cases into proportions. The fraction of decisions issued by Delaware judges fell steadily, from 80% in 1995 to an average of 31% over 2005–2009. The percentage decided in other state courts increased somewhat, but the principal growth was in the fraction of decisions in federal courts.

on when judges should write opinions).

Figure 2: Proportion of Corporate Law Decisions Involving Delaware Companies by Location, 1995–2009



Proportion of cases involving suits under corporate law against directors of Delaware public companies by location, for cases with one or more reported decisions on Westlaw, Lexis, or the Delaware Chancery Court website, with the first reported decision issued between 1995 and 2009.

Our judicial opinions dataset provides *prima facie* evidence that Delaware courts have suffered a major drop in market share in producing corporate law jurisprudence. Still, focusing on publicly-available judicial opinions provides only a partial view of underlying trends. Cases that lead to written decisions may not be representative of all cases that are filed.[45] Cases with decisions must be serious enough for a judge to take the time to write an opinion, and Lexis or Westlaw must then deem the opinion to be sufficiently important to merit dissemination. Also, in many states, most trial court decisions are not published.[46] For appellate rulings, many states either have a presumption against publication or reserve publication for cases that establish a new rule, modify or criticize an existing legal rule, or involve an issue of continuing public interest.[47]

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45. For criticisms of research that relies solely on reported decisions, see, for example, Erickson (2010), *supra* note 10, at 1753–54; David A. Hoffman, Alan J. Izenman & Jeffrey R. Lidicker, *Docketology, District Courts, and Doctrine*, 85 WASH. U. L. REV. 681, 688–89 (2007); Pauline T. Kim, Margo Schlanger, Christina L. Boyd & Andrew D. Martin, *How Should We Study District Judge Decision-Making?*, 29 WASH. U. J.L. & POL'Y 83, 96–97 (2009).

46. Peter W. Martin, *Reconfiguring Law Reports and the Concept of Precedent for a Digital Age*, 53 VILL. L. REV. 1, 17–18, 31, 34–35 (2008) (noting that this tradition emerged when cases were reported in print and selectivity was required because published law reports were costly to produce, distribute, and store).

47. Jane Williams, *Survey of State Court Opinion Writing and Publication Practices*, 83 LAW LIBR. J. 21, 22 (1991).

2. Large Mergers and Acquisitions

To respond to the limitations of research based on reported cases, we investigated cases filed. There is no data source that would let us find all corporate suits filed, in federal court and all 50 states. We therefore focused on three key categories of cases where it was feasible to identify suits filed: large mergers and acquisitions, leveraged buyouts, and instances where corporate executives allegedly benefitted from options backdating.

Mergers and acquisitions ("M&A") transactions account for a large fraction of corporate lawsuits involving public companies.[48] Accordingly, we studied filings relating to the 25 largest completed M&A transactions for each year from 1994 to 2009, measured by transaction value, where the acquired company was based in the United States and publicly traded, to find out whether shareholder lawsuits had been filed and, if so, where.[49] Of the 400 target companies, 395 had filings available on the SEC's EDGAR database, and 256 of these were incorporated in Delaware. We searched these companies' filings and found takeover-related shareholder suits under corporate law against the target and/or its board for 121 of these 256 firms (47%).

Figure 3 summarizes when and where the suits involving the 121 Delaware targets were filed.[50] The average number of suits was about 18 per year, with a surge beginning around 2004, consistent with press reports that M&A litigation was increasing.[51] Through 2001, most suits were filed in Delaware. From that point onwards, the non-Delaware share has grown substantially.

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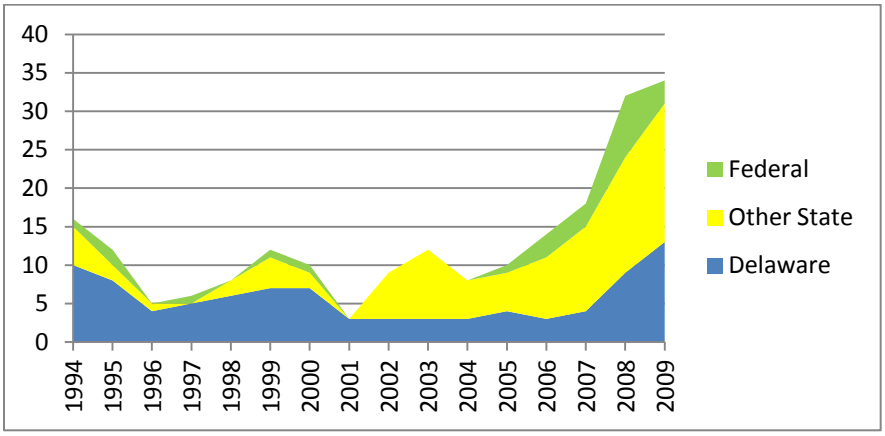
48. Robert B. Thompson & Randall S. Thomas, *The New Look of Shareholder Litigation: Acquisition-Oriented Class Actions*, 57 VAND. L. REV. 133, 169 tbl.2 (2004) (during 1999 and 2000 a total of 952 fiduciary suits were brought in Delaware courts where a public company was involved, and 796—nearly 80%—of these lawsuits involved acquisitions).

49. We used the SDC Platinum database, accessed through Thomson One Banker. We excluded leveraged buyouts, which we investigate separately. The data reported in this Article for large M&A and LBO transactions extend through 2009; the results in *ABC Losing Cases* (2012), *supra* note 5, extend through 2010 but are otherwise consistent.

50. We treated multiple suits in any given jurisdiction as one suit, whether or not these suits were formally consolidated. In the federal courts, Delaware courts, and most other state courts, multiple suits in the same jurisdiction involving similar facts typically will be consolidated and the court will appoint a lead plaintiff(s) and law firm(s), at least if the case proceeds beyond an early stage.

51. Ken MacFadyen, *A Low Plaintiffs Bar?*, MERGERS & ACQUISITIONS: THE DEALMAKERS J., Oct. 2010, at 22; Dionne Searcey & Ashby Jones, *First, the Merger; Then the Lawsuit*, WALL ST. J. ONLINE (Jan. 10, 2011), http://online.wsj.com/article/SB10001424052748704482704576072050216781160.html?mod=rss.

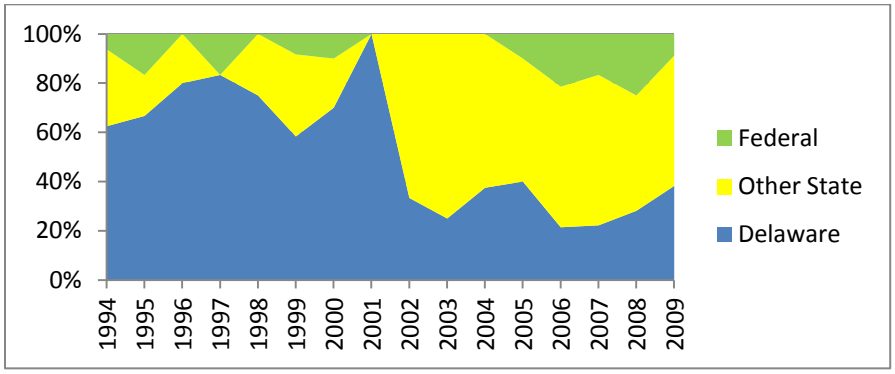
Figure 3: Corporate Lawsuits Involving 25 Largest M&A Transactions by Location, 1994–2009



Suits under corporate law against Delaware public companies that were acquired in the largest 25 M&A transactions in each year, by location of suit, 1994–2009. One or more suits in a single jurisdiction are treated as a single suit.

Figure 4 turns the large-deal M&A case counts into percentages and further confirms the out-of-Delaware trend. Between 1994 and 2001, 69% of the suits were filed in Delaware. From 2002 onward, this average dropped to 31%.

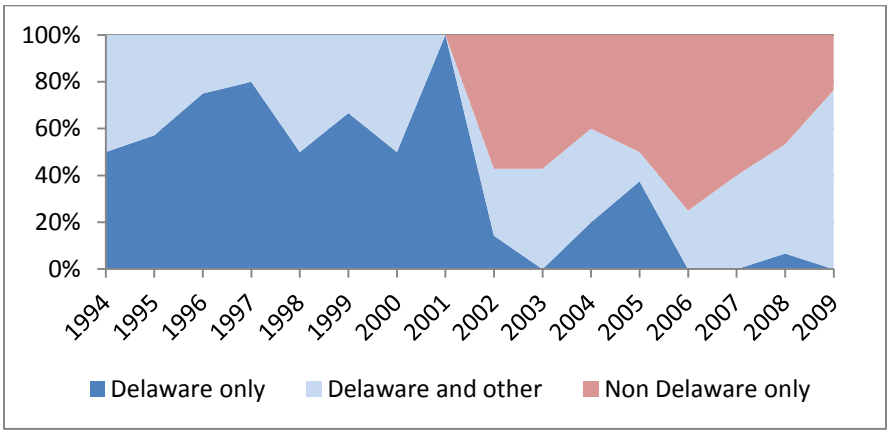
Figure 4: Proportion of Corporate Lawsuits Involving 25 Largest M&A Transactions by Location, 1994–2009



Proportions of suits under corporate law against Delaware public companies that were acquired in the largest 25 M&A transactions in each year, by location of suit, 1994–2009. One or more suits in a single jurisdiction are treated as a single suit.

A related trend is that, while it used to be common for suits in cases arising from large M&A transactions to be filed *only* in Delaware, this has become rare. As Figure 5 indicates, through 2001, Delaware was always *a* forum in corporate lawsuits arising from the 25 largest M&A transactions and often was the sole forum. From 2002 onwards, Delaware was rarely the sole forum. Indeed, from 2006 to 2009, Delaware was the sole venue exactly once, and, in almost half of litigated major takeovers, Delaware was not a forum at all.

Figure 5: Proportion of 25 Largest M&A Transactions with Lawsuits Filed in Delaware Only, Delaware and Elsewhere, and Only Outside Delaware, 1994–2009



For the largest 25 M&A transactions in each year with a Delaware-incorporated target and at least one suit filed under corporate law, locations of suits (Delaware only, Delaware plus another forum, or outside Delaware only), 1994–2009. One or more suits in a single jurisdiction are treated as a single suit.

Several recent studies confirm that out-of-Delaware suits challenging takeovers are common with Delaware companies. Brian Quinn examined the litigation venue for 119 mergers occurring between August 2009 and August 2010 with a public Delaware target and a transaction value of at least $100 million.[52] Of the 97 deals with deal-related litigation, Delaware was the sole forum only 8 times. For 41 of the 97 litigated deals, all suits were filed outside Delaware. Jennifer Johnson found 196 instances in 2010 where class actions were filed under state corporate law involving Delaware public companies, of which 193 involved M&A transactions.[53] These 196 class actions gave rise to 265 suits, of which 103 (39%) were brought in Delaware, 115 in other state courts, and 47 in federal court. Thus, for 93 of the Delaware firms (47%), the plaintiffs sued only outside Delaware. Matthew Cain and Steven Davidoff studied 955 takeovers with a transaction value of over $100 million completed between 2005 and 2010, and found shareholder suits in 475 deals (50%). They do not report how many suits involve Delaware companies, but their data indirectly shows the extent of the out-of-Delaware trend. Of 322 cases which settled, only 90 (28%) were settled in Delaware courts even though 595 of the 955 targets (62%) were Delaware companies.[54]

3. Leveraged Buyout Transactions

To provide a different window into M&A litigation trends, we studied leveraged buyouts ("LBOs") of public companies. Many significant recent Delaware cases involve these going-private transactions, which are litigation prone, and for good reason. Insiders will often be, or expect to be, on the side intending to take the company private, in which case they will prefer a lower price.[55] Shareholder plaintiffs (and their lawyers) understandably will wonder if, or how strongly, the board will seek to maximize the takeover price.[56]

As with large M&A transactions, we obtained data for LBOs from the SDC Platinum database, relying on their "leveraged buyouts" category. We found 511 LBOs of public companies announced and completed between 1995 and 2009. Of these, 477 had filings on EDGAR and 300 of those 477 (63%) were incorporated in Delaware. We found corporate litigation for 141 (47%) of the 300 Delaware targets, all from 1997 onwards.[57] Figure 6 indicates when and where these suits were filed.

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52. Quinn (2011), *supra* note 10, at 9.

53. Johnson (2012), *supra* note 10, at 37. Johnson refers to these suits as "state securities class actions." *Id.* However, the suits she studies arise under corporate law, not "securities law." *Id.*

54. Cain & Davidoff (2012), *supra* note 10, at 31–32 tbl.1, 35 tbl.3.

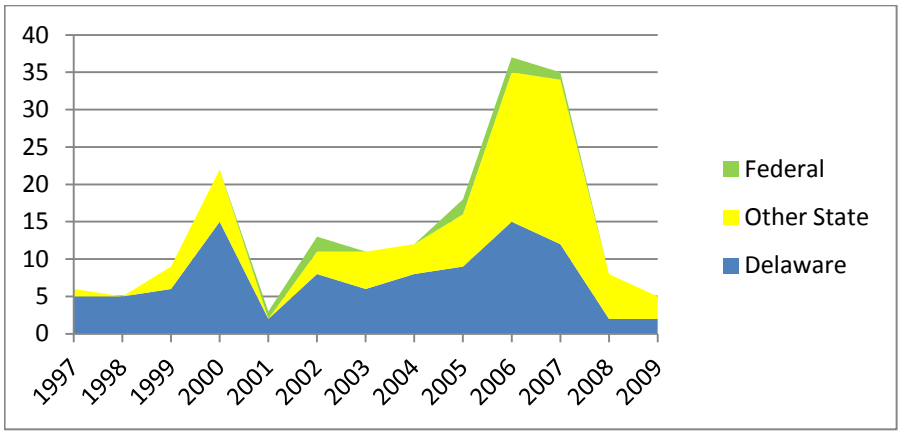
55. As Chancellor Strine observed in *In re The Topps Co. S'holders Litig.*, 924 A.2d 951, 963 (Del. Ch. 2007), "Few contexts are more important to stockholders than the pendency of a transaction in which they exchange their shares for cash and the company is taken private."

56. Randall Chase, *Delaware Judges Want Say in Private Equity Liability Cases*, INSURANCE J. (May 22, 2007), http://www.insurancejournal.com/news/east/2007/05/22/79917.htm.

57. Part of the reason there were no LBOs in our dataset for 1995 and 1996 was that

Figure 6 shows that the number of LBO-related suits rises and falls with market cycles in private equity buyouts, which were common during the late 1990s and boomed in the mid-2000s.[58] With respect to where the lawsuits were filed, the pattern Figure 6 reveals is, by now, familiar. Most suits challenging LBOs by Delaware companies were filed in Delaware through 2002, and other venues grew in popularity thereafter. From 1997 to 2001, 73% of LBO suits involving Delaware companies were in Delaware. For 2002 to 2009, the equivalent figure was only 45%.

Figure 6: Corporate Lawsuits Involving Leveraged Buyouts in Delaware, Other States, and Federal Courts, 1997–2009



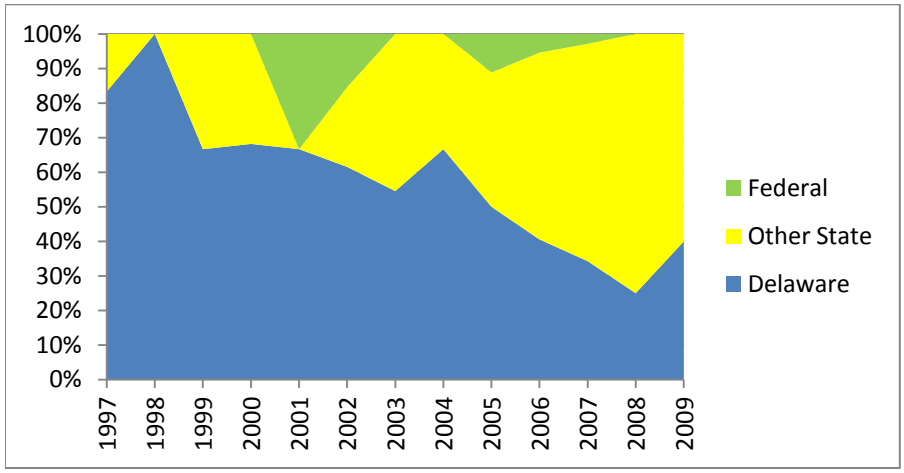
Suits under corporate law against Delaware public companies acquired in leveraged buyouts in each year, by location of suit, 1997–2009. One or more suits in a single jurisdiction are treated as a single suit.

Figure 7 translates the LBO case count into percentages. It reveals that as cases were increasingly brought outside Delaware, other state courts were typically the venue chosen.

public company LBOs were not common during those years. *See* Brian Cheffins & John Armour, *The Eclipse of Private Equity*, 33 DEL. J. CORP. L. 1, 20 fig.1 (2008). Also, LBO targets are smaller than the targets in our "large" M&A dataset, so targets in 1995 and 1996 may have been too small to appear on EDGAR, a system that was then being phased in. *Office of Interactive Disclosure: History*, U.S. SEC. & EXCHANGE COMMISSION (Jan. 8, 2010), http://www.sec.gov/spotlight/xbrl/oid-history.shtml. The median transaction value in our LBO dataset was $1.55 billion, versus $13.33 billion for our mega-deal dataset.

58. For general trends with LBO activity, see Cheffins & Armour (2008), *supra* note 57, at 20 fig.1, 22–24.

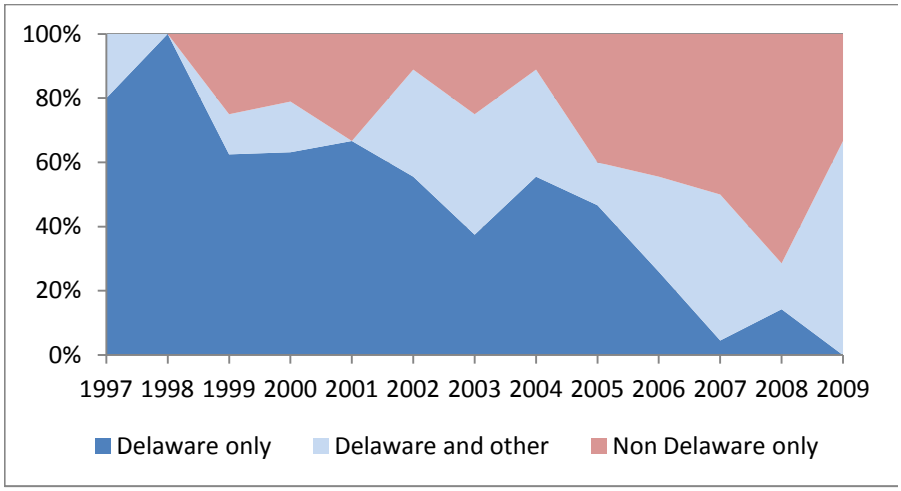
Figure 7: Proportion of Suits Involving Leveraged Buyouts in Delaware, Other States, and Federal Courts, 1997–2009



Proportions of corporate lawsuits against Delaware public companies acquired in leveraged buyouts in each year by location of suit, 1997–2009. One or more suits in a single jurisdiction are treated as a single suit.

With LBOs, as with large M&A transactions, it was common in the early part of our study period for lawsuits to be filed *only* in Delaware, but this subsequently became rare. As Figure 8 indicates, while between 1997 and 2002 Delaware was the only forum in which LBO suits were filed in 66% of transactions with lawsuits, this figure dropped to 26% between 2003 and 2009. Between 2007 and 2009 only two LBOs involved "Delaware only" litigation. Likewise, while lawsuits were filed solely outside Delaware in only 18% of LBOs from 1997 to 2002, this figure grew to 41% between 2003 and 2009. Hence, our LBO data confirms a robust out-of-Delaware trend.

Figure 8: Proportion of Leveraged Buyouts with Lawsuits Filed in Delaware Only, Delaware and Elsewhere, and Only Outside Delaware, 1997–2009



For leveraged buyouts in each year, with a Delaware-incorporated target and at least one suit under corporate law, locations of suits (Delaware only, Delaware plus another forum, or outside Delaware only), 1997–2009. One or more suits in a single jurisdiction are treated as a single suit.

4. Options Backdating Cases

Corporate suits involving takeovers are usually direct suits, generally filed as class actions, rather than derivative suits.[59] To round out our analysis of where corporate suits are filed, we turn next to options backdating cases, which were typically brought as derivative suits.[60] These suits arose out of allegations that largely came to light in 2005 and 2006. The standard pattern was that companies granted stock options with an exercise price based on a trading price from an earlier date which was below the market price at the date of grant and then claimed they had issued the options with an "at market" exercise price.[61] Options backdating was a major public scandal, which led to many restatements of financial results, many civil lawsuits and settlements, a number of SEC investigations, and a few criminal convictions.[62] The civil lawsuits rested on apparent self-dealing and, as both our

59. Thompson & Thomas (2004), *supra* note 48, at 168.

60. The other possibility, for companies which restated their financial results, was a securities class action suit, but plaintiffs' lawyers pursued this option less often because many options backdating announcements did not produce a sharp drop in the share price, typically a key element in a successful securities law class action. *See* Paul Sweeney, *Legal Niceties Color Backdating Cases*, FIN. EXECUTIVE, July–Aug. 2007, at 33.

61. Christy L. Abbott, *The Shareholder Derivative Suit as a Response to Stock Option Backdating*, 53 ST. LOUIS U. L.J. 593, 597–99 (2009).

62. Timothy P. Stone, *The Rise and Fall of Options Backdating: From Executive Windfall to Executive Pitfall*, 76 DEF. COUNS. J. 174 (2009). On the SEC investigations, see Stephen J. Choi, A.C. Pritchard & Anat Carmy Wiechman, Scandal Enforcement at the SEC: Salience and the Arc of the Option Backdating Investigations (Sept. 1, 2011) (unpublished manuscript), *available at* http://ssrn.com/abstract=1876727.

plaintiff and defense lawyer interviewees advised us, many were seen as offering good prospects for monetary recoveries.[63]

We relied on a variety of sources to identify 165 companies whose directors faced options backdating derivative lawsuits and investigated these suits.[64] Of these companies, 127 (77%) were incorporated in Delaware. For these 127 firms, we found 234 derivative lawsuits, of which only 26 (11%) were filed in Delaware. Delaware was the sole forum for suits involving only four companies. About half of these 234 cases (115) were filed in federal court (normally relying on diversity jurisdiction), and the other 93 cases were filed in state court in a state other than Delaware. An important wave of corporate litigation thus largely bypassed the Delaware courts. A study by Jessica Erickson of derivative suits filed in federal court over a one year period during 2005–2006 indicates that derivative suits involving allegations other than options backdating are also often filed in federal court. The filing rate she found was substantially higher than prior studies had found for derivative suits filed in Delaware.[65]

C. Anecdotal Evidence

Our quantitative evidence shows clearly that while plaintiffs' lawyers traditionally preferred to launch suits involving Delaware companies in Delaware court, they now often sue in federal court or another state court for derivative suits and in another state court for direct (typically class action) suits. Delaware now rarely exercises full control over corporate litigation, in the sense of being the sole forum. In many cases, it never sees the litigation at all.

Anecdotal evidence supports our empirical findings. Our interviews with plaintiffs' and defense lawyers confirmed awareness of a growing tendency on the part of plaintiffs' lawyers to file outside Delaware. Moreover, over the past few years, commentators have remarked upon an erosion of Delaware's litigation dominance.[66] For instance, in 2007, Ted Mirvis, a litigation partner in the well-known Wachtell Lipton law firm, referred to an "Anywhere But Chancery" trend, with "Chancery" being the Delaware Chancery Court.[67] Likewise, a New York City Bar Association Committee noted in a 2008 report that it had become "common" for shareholder suits in M&A transactions to be filed in multiple jurisdictions.[68]

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63. Amanda Bronstad, *Backdating Cases Head to Settlement*, NAT'L L.J., Feb. 18, 2008, at 1.

64. For details, see *ABC Losing Cases* (2012), *supra* note 5, at 23–27.

65. Erickson (2010), *supra* note 10, at 1757, 1761–62. Though Erickson did not focus exclusively on publicly traded companies, most of the suits she studied involved such companies. *Id.* at 1770.

66. *See, e.g.*, David Marcus, *Did Chancery Fee Rulings Chase Away Plaintiffs Lawyers?*, DEL. L. WKLY., Nov. 29, 2006, at 1; Ken MacFadyen, *Delaware Ruling Alters M&A Landscape*, INVESTMENT DEALERS DIG., Apr. 16, 2007, at 3; Elizabeth Bennett, *Delaware Keeps Its Pre-Eminence in Business Litigation*, DEL. L. WKLY., May 2, 2007, at 1 (citing views of Chief Justice Myron Steele of the Delaware Supreme Court).

67. *Anywhere but Chancery* (2007), *supra* note 1.

68. COMMITTEE ON SECURITIES LITIGATION, ASSOCIATION OF THE BAR OF THE CITY OF NEW YORK, COORDINATING RELATED SECURITIES LITIGATION: A POSITION PAPER 3 (2008).

Further evidence comes from a recent uptick in companies adopting bylaws or charter provisions making Delaware the preferred forum for corporate suits, a trend we discuss in Part V.

III. WHAT HAS PROMPTED THE OUT-OF-DELAWARE TREND?

The out-of-Delaware trend raises questions concerning causes, potential cures, and its consequences for Delaware's pre-eminence.[69] The remainder of the Article addresses these topics. In this Part, we assess the potential causes of the trend.

A. Who Decides Where Lawsuits Are Brought?

From among the available fora, plaintiffs choose where to sue. As a practical matter, the forum choice for representative litigation under corporate law (either a derivative suit or a class action suit)[70] will usually be made by the law firms acting on behalf of plaintiffs, with little or no client input.[71] Lawyers can only sue where they are permitted to practice, but Delaware readily accommodates out-of-state counsel, so this is not a major constraint on the choice of venue.[72]

To be sure, if suits are filed in more than one forum, the defendants can move to stay in one forum, in favor of their preferred forum. These motions are made with some frequency, but far from all of the time. When made, they do not always succeed.[73] Moreover, defense counsel may sometimes prefer sidetracking Delaware

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The Committee focused on the multiplication of suits, rather than their location. *Id.* at 1–2.

69. *See supra* note 3 and accompanying text.

70. On derivative actions and shareholder class actions qualifying as representative litigation, see Amy M. Koopmann, *A Necessary Gatekeeper: The Fiduciary Duties of the Lead Plaintiff in Shareholder Derivative Litigation*, 34 J. CORP. L. 895, 899 (2009).

71. On plaintiffs lawyers' control over this choice, see Jonathan R. Macey & Geoffrey P. Miller, *The Plaintiff's Attorney's Role in Class Action and Derivative Litigation: Economic Analysis and Recommendations for Reform*, 58 U. CHI. L. REV. 1, 19–20 (1991); John C. Coffee, Jr., *Understanding the Plaintiff's Attorney: The Implications for Economic Theory for Private Enforcement of Law Through Class and Derivative Actions*, 86 COLUM. L. REV. 669, 679–84 (1986); Randall S. Thomas & Robert G. Hansen, *Auctioning Class Action and Derivative Lawsuits: A Critical Analysis*, 87 NW. U. L. REV. 423, 433 (1993).

72. *See* DEL. STATE BAR ASS'N, REPORT OF THE MULTIJURISDICTIONAL PRACTICE SPECIAL COMMITTEE TO DENNIS L. SCHRADER, ESQUIRE, PRESIDENT, DELAWARE STATE BAR ASSOCIATION 2, 10 (2001), *available at* http://www.dsba.org/pdfs/MJPReport.pdf (indicating the system in place was working well and that numerous out-of-state lawyers were routinely given permission to litigate in Delaware courts).

73. We studied stay applications and their outcomes for our options backdating dataset. Of the 97 companies which faced backdating derivative suits in two or more jurisdictions, 31 (32%) reported that there had been a motion granted to stay in favor of another jurisdiction or a motion to remove a case from state court to federal court. Of these 31 companies, 24 were Delaware companies. Three other companies (two of which were Delaware firms) had stay motions which were denied; one further Delaware company had a motion which was reported as pending. Since we relied on company 10-Ks as the principal source of information about stay motions, we might have missed some motions, especially unsuccessful ones, which companies might not have reported.

proceedings in favor of a competing forum.[74] Indeed, if federal diversity jurisdiction is available, a defendant may remove the case to federal court as of right.[75] Thus, stay motions reduce, but far from eliminate, the impact of out-of-Delaware choices by plaintiffs' lawyers. We therefore explore in this section the principal reasons why plaintiffs' lawyers are making different choices today than 15 years ago.

B. Predictability, Pro-Defendant Bias, and the Time Dimension

Ted Mirvis, the Wachtell Lipton litigation partner, has suggested that corporate lawsuits have "greater settlement value outside of Delaware" due to greater variation in possible outcomes.[76] He points out that outcomes in Delaware are reasonably predictable due to the rich body of precedents and the judiciary's familiarity with the conduct expected of the principal corporate actors. Plaintiffs' attorneys therefore have little scope to seek a generous settlement by relying on the possibility of a disastrous trial outcome. Plaintiffs' lawyers, according to Mirvis, have greater leverage outside Delaware due to the risk that a non-Delaware judge or jury will grant inappropriately generous relief.

These conjectures are plausible, but cannot, without more, explain the time trend we document. Greater certainty would have been a feature of Delaware litigation 15 years ago, as much as today.[77] Thus, even if litigation (un)certainty partly explains why plaintiffs' lawyers may prefer a non-Delaware forum, this factor cannot readily explain why they sue outside Delaware far more often today than in the 1990s.

A similar difficulty arises with a second plausible explanation for plaintiffs filing outside Delaware—Delaware judges favor corporate defendants.[78] Some plaintiffs' lawyers we interviewed told us that the likelihood of appearing before a sympathetic judge is one factor in deciding where to file. Empirical research on choice of forum confirms that attorney perceptions of judicial predispositions strongly influence where cases are filed.[79] As a result, a perceived pro-manager bias

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74. For examples, see *In re* Bear Stearns Cos. Inc. S'holder Litig., C.A. No. 3643–VCP, 2008 WL 959992 (Del. Ch. Apr. 9, 2008), *available at* 33 Del. J. Corp. L. 515 (2008) (defendants moving to stay Delaware action in favor of New York actions); Transcript of Courtroom Status Conference, Scully v. Nighthawk Radiology Holdings Inc., No. 5890–VCL, (Del. Ch. Dec. 17, 2010) (hearing on proposed dismissal of Delaware suit in anticipation of a court-approved settlement in Arizona courts).

75. 28 U.S.C. § 1441 (2006).

76. *Anywhere but Chancery* (2007), *supra* note 1, at 17; *see also* Micheletti & Parker (2012), *supra* note 10, at 6–7.

77. Certainty has been cited as a virtue of Delaware law for over two decades. *See, e.g.*, Macey & Miller (1987), *supra* note 25, at 484; ROMANO (1993), *supra* note 15, at 39–40; Demetrios G. Kaouris, *Is Delaware Still a Haven for Incorporation?*, 20 DEL. J. CORP. L. 965, 977 (1995).

78. Mark Lebovitch, Jerry Silk & Jeremy Friedman, *Improving Multi-Jurisdictional, Merger-Related Litigation*, ABA COMMERCIAL & BUS. LITIG. COMM., Feb. 14, 2011, at 1, *available at* http://apps.americanbar.org/litigation/committees/commercial/articles.html (reporting that many plaintiffs' lawyers "perceive Delaware as less shareholder-friendly").

79. Thomas E. Willging & Shannon R. Wheatman, *Attorney Choice of Forum in Class*

could cause plaintiffs' lawyers to avoid the Delaware courts.[80] But the claim that the Delaware courts favor management is an old one. For example, William Cary complained in 1974 that the Delaware courts had "watered the rights of shareholders vis-à-vis management down to a thin gruel."[81] Yet Delaware's dominance of corporate litigation has eroded only recently.

Pro-manager bias could account for the out-of-Delaware trend our data reveals if this bias is greater now than formerly. Is this the case? Norman Veasey, former chief justice of the Delaware Supreme Court, does not think so. He observed in a 2005 survey of Delaware case law that "Delaware courts today are not any more 'pro-stockholder' and less 'pro-director' or 'pro-manager' than they were in the past, or vice versa."[82]

Our own sense is that the Delaware courts are not significantly more pro-manager today than in the 1990s. There have been, to be sure, some moves in Delaware toward greater deference to management. The Delaware courts have watered down the board's *Revlon* duty in the takeover context to seek the highest price reasonably available by allowing a broad range of board processes to satisfy this duty.[83] They have also announced a tough "conscious disregard" of duty standard for finding that outside directors acted in bad faith and hence are not protected by a section 102(b)(7) charter provision exempting directors from monetary liability[84]—and they have never found this standard to be met.[85] Still, in broader terms, the Delaware courts were attentive to self-dealing in the 1990s and

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Action Litigation: What Difference Does It Make?, 81 NOTRE DAME L. REV. 591, 611 (2006).

80. Stevelman (2009), *supra* note 10, at 97.

81. Cary (1974), *supra* note 2, at 666; *see also* William M. Lafferty & W. Leighton Lord III, *Towards a Relaxed Summary Judgment Standard for the Delaware Court of Chancery: A New Weapon Against "Strike" Suits*, 15 DEL. J. CORP. L. 921, 928 (1990); Renee M. Jones, *Rethinking Corporate Federalism in the Era of Corporate Reform*, 29 J. CORP. L. 625, 645–54 (2004).

82. E. Norman Veasey & Christine T. Di Guglielmo, *What Happened in Delaware Corporate Law and Governance from 1992–2004? A Retrospective on Some Key Developments*, 153 U. PA. L. REV. 1399, 1496 (2005).

83. Revlon, Inc. v. MacAndrews & Forbes Holdings, Inc., 506 A.2d 173 (Del. 1986). For an example of the discretion given to target boards, see *In re* Toys "R" Us, Inc. S'holder Litig., 877 A.2d 975 (Del. Ch. 2005). One of our defense counsel interviewees cited *Toys "R" Us* as a spur for plaintiffs' preference to file outside Delaware.

84. *In re* Walt Disney Co. Derivative Litig., 906 A.2d. 27, 62–67 (Del. 2006).

85. The most recent Chancery Court decision that let such a claim survive a motion for summary judgment was reversed by the Delaware Supreme Court. *See* Ryan v. Lyondell Chem. Co., C.A. No. 3176–VCN, 2008 WL 2923427 (Del. Ch. July 29, 2008), *rev'd*, 970 A.2d 235 (Del. 2009).

remain so.[86] Moreover, absent self-dealing, they rarely disturbed board decisions then, and rarely do so today.[87]

Some of the plaintiffs' lawyers we interviewed, however, believe that the Delaware courts have become more defendant friendly in various ways. They told us that some Delaware judges presume that any case brought is weak, until proven otherwise. Several stressed the need to build credibility with the Delaware judges by bringing good cases, and only good cases.[88] Others reported difficulty getting judicial approval for expedited discovery, even in cases with apparently strong facts. Another complaint was that it was hard to get a preliminary injunction hearing in merger cases until shortly before the shareholder vote, when there was almost no chance the judge would delay the vote.

Our judgment, developed next, is that the Delaware courts' increasingly skeptical view of the plaintiffs' bar did more to foster the out-of-Delaware trend than any increase in pro-defendant bias. Still, perceived pro-defendant bias could have contributed indirectly to the out-of-Delaware trend. Once plaintiff firms had other reasons to file elsewhere, and became comfortable with doing so, a sense that Delaware judges favor management, perhaps more than judges elsewhere, could provide an additional reason for filing outside Delaware.

C. Judicial Attitudes Concerning the Plaintiffs' Bar

Various recent utterances and rulings by Delaware judges suggest a jaundiced view of at least some members of the plaintiffs' bar. These misgivings could lead some law firms to hesitate before filing in Delaware courts. Judicial skepticism toward the plaintiffs' bar could be related to a general pro-management orientation, but could also exist separately. Judges might believe that suits that target true managerial misfeasance are, as Chancellor Chandler said in *In re Fuqua Industries, Inc. Shareholder Litigation*, "a cornerstone of sound corporate governance"[89] and yet still believe that attorneys who bring weak cases do judges, executives, directors, and stockholders a disservice. Various opinions, especially by Chancellor Strine and Vice Chancellor Laster, conform to this point of view.

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86. On scrutiny of self-dealing, see Edward B. Rock, *Saints and Sinners: How Does Delaware Corporate Law Work?*, 44 UCLA L. REV. 1009, 1015 (1997) ("Directors of Delaware corporations can do anything they want, *as long as* it is not illegal, and as long as they act in good faith." (emphasis added)). For a recent example, see *In re* S. Peru Copper Corp. S'holder Derivative Litig., 30 A.3d 60 (Del. Ch. 2011) (awarding $1.26 billion in damages from related party transaction), *opinion revised and superseded*, C.A. No. 961–CS, 2011 WL 6440761 (Del. Ch. Dec. 20, 2011).

87. For recent confirmation of the Delaware courts' reluctance to overrule board decisions absent self-dealing, see Air Prod. & Chem., Inc. v. Airgas, Inc., 16 A.3d 48 (Del. Ch. 2011) (upholding continued use of "poison pill" defense by Airgas board after losing proxy context brought by hostile bidder).

88. One plaintiffs' lawyer told us that his firm would drop a case brought in Delaware if the supporting facts turned out to be weak, rather than pursue the modest settlement that those facts might support. Another advised that he would bring strong cases in Delaware, but weaker ones, where he hoped to "free ride" on parallel securities litigation, elsewhere.

89. 752 A.2d 126, 133 (Del. Ch. 1999).

In re Cox Communications, Inc. Shareholders Litigation, a 2005 case, illustrates the doubts expressed about the plaintiffs' bar.[90] Chancellor Strine, while ruling that plaintiffs' attorneys who settled a class action lawsuit over a going-private transaction should receive only one quarter of the $5 million in fees they had requested and to which the defendants had not objected, expressed misgivings about both shareholder class actions and the plaintiffs' bar. He criticized in particular the tendency for a takeover announcement to prompt "hastily-filed, first-day complaints that serve no purpose other than for a particular law firm and its client to get into the medal round of the filing speed (also formerly known as the lead counsel selection) Olympics."[91] He continued:

> Particularly in the representative litigation context, where there are deep concerns about the agency costs imposed by plaintiffs' attorneys, our judiciary must be vigilant to make sure that the incentives we create promote integrity and that we do not, by judicial doctrine, generate the need for defendants to settle simply because they have no viable alternative, even when they have done nothing wrong.[92]

Chancellor Strine acknowledged that shareholder suits are an important check against director wrongdoing.[93] Nevertheless, his skeptical words could have given some plaintiffs' lawyers reason to file elsewhere.[94] The effect would have been magnified by his fee cut. Various plaintiffs' lawyers we interviewed cited *Cox Communications* as an important reason to avoid Delaware.

Various decisions by Vice Chancellor Laster also betray doubts about many shareholder suits and some plaintiffs' law firms. In *In re Revlon, Inc. Shareholders Litigation*, he took control of a case involving a going-private transaction away from lead counsel, finding that the lawyers had failed to provide adequate representation.[95] In so doing Vice Chancellor Laster wrote that the current litigation system "generates questionable benefits for class [action suit] members, provides transaction-wide releases for defendants, and offers a good living for the traditional plaintiffs' bar."[96] In *In re Compellent Technologies*, multiple class actions were filed alleging breaches of duty by Compellent's directors in selling the company and a motion was brought to consolidate the various proceedings. Vice Chancellor Laster observed, when seeking further information from the contending law firms, that "the whole problem is the diversion of interests between entrepreneurial plaintiffs' counsel and the class. You all maximize by getting the most fee for the least work."[97]

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90. 879 A.2d 604 (Del. Ch. 2005); *see also, e.g.*, *In re* Revlon, Inc. S'holders Litig., 990 A.2d 940 (Del. Ch. 2010).

91. *In re* Cox Commc'ns Inc., S'holders Litig., 879 A.2d at 608; *see also id.* at 614–23, 642–48.

92. *Id.* at 643.

93. *Id.*

94. *See* David Marcus, *State of Denial*, DAILY DEAL, Nov. 20, 2006 (available through LexisNexis Academic using search terms "State of Denial").

95. *In re* Revlon, Inc. S'holders Litig., 990 A.2d at 961.

96. *Id.* at 959–60.

97. Transcript of Plaintiffs' Motion for a Preliminary Injunction & the Court's Ruling at

In *Scully v. Nighthawk Radiology Holdings*, where Vice Chancellor Laster was asked to approve a settlement that would shut down litigation in Delaware in favor of a parallel Arizona case, he cast aspersions on takeover-related suits, saying "a lot of these sue-on-every-deal cases are . . . worthless, they're simply we see the announcement, then we file, okay?"[98] He ordered an investigation by special counsel of possible collusion between plaintiffs' and defense lawyers, and suggested that he might bar David Berger, a senior partner at Silicon Valley-based Wilson, Sonsini, Goodrich & Rosati, from practicing in Delaware courts. The investigation generated considerable concern among both the defense and plaintiffs' bar,[99] but the special counsel recommended against any sanction.[100]

Despite his sharp criticism of the plaintiffs' bar, Vice Chancellor Laster insists he is not pro-defendant.[101] His apparent view is that good cases should be vigorously pursued and bad cases should not be brought, at least not in Delaware. He will praise plaintiffs' lawyers too, saying in a 2010 hearing where he declined to enjoin a bid by Fairfax Financial Holdings Ltd. to acquire Zenith National Insurance Corp. that "[t]his was a well-litigated, well-presented case. It's one the plaintiffs were justified in bringing."[102] Likewise, in *Landry's Restaurants*, Vice Chancellor Laster approved a $12 million fee award, calling the settlement "excellent" and the fee "reasonable and . . . well earned."[103]

The more "pro-Delaware" plaintiffs' lawyers we interviewed were generally proud of the quality of the cases they bring and maintained they were not too discomfited by what Chancellor Strine and Vice Chancellor Laster have said. Yet harsh words, directed at much of the plaintiffs' bar, are likely to discourage filing in Delaware. Several of the plaintiffs' lawyers we interviewed cited this sort of rhetoric to support their Delaware-skeptical views. As a 2011 news report said of Vice Chancellor Laster, "Lawyers . . . understandably might want to avoid the newest judge on one of the top U.S. business courts."[104]

Judicial skepticism toward the plaintiffs' bar is a relatively recent phenomenon in Delaware, and its timing is consistent with erosion of the state's litigation market share. Delaware has traditionally been seen as litigation friendly, with the Delaware corporate bar allegedly supporting an "easy to sue" system that ensured business for Delaware lawyers in an otherwise "pro-manager" state.[105] Joseph Bishop said of Delaware more than forty years ago, "Delaware's general approach to stockholder

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*7, *In re* Compellent Tech., Inc. S'holder Litig., C.A. No. 6084–VCL (Del. Ch. Jan. 13, 2011).

98. Courtroom Status Conference at 16, Scully v. Nighthawk Radiology Holdings, C.A. No. 5890–VCL (Del. Ch. Dec. 17, 2010).

99. Amy Kolz, *Rigging the Game?*, AM. LAW., Mar. 1, 2011, at 13.

100. Brief of Special Counsel Gregory P. Williams at 41, Scully v. Nighthawk Radiology Holdings, Inc., C.A. No. 5890–VCL (Del. Ch. Mar. 11, 2011).

101. *Judge Rattles Lawyers in U.S. Shareholder Battles*, HEDGEWORLD DAILY NEWS, Feb. 11, 2011.

102. David Marcus, *Mixed Message*, THE DEAL MAGAZINE (June 4, 2010), http://www.thedeal.com/magazine/ID/034577/insights/safe-harbor/mixed-message.php.

103. Transcript of Settlement Hearing at 21, 25, Louisiana Mun. Emps.' Ret. Sys. v. Fertitta, C.A. No. 4339–VCL (Del. Ch. Oct. 6, 2010).

104. *Judge Rattles Lawyers in U.S. Shareholder Battles* (2011), *supra* note 101.

105. Cary (1974), *supra* note 2, at 686–88; Macey & Miller (1987), *supra* note 25, at 510–13.

litigation . . . is to make it easy to sue the executives of Delaware corporations, no matter where they reside or the corporation does business, so long as the suit is in Delaware courts, and conducted by Delaware counsel."[106] Douglas Branson said similarly about twenty years ago, "Delaware makes suit in Delaware the obvious choice."[107] The rhetoric in cases like *Cox Communications*, *Revlon*, and *Scully* is a marked departure from this litigation-friendly posture and plausibly contributed to the out-of-Delaware trend.

D. Attorneys' Fees

Cases such as *Cox Communications* and *Revlon* are troubling for plaintiffs' lawyers quite apart from their rhetoric. In *Cox Communications*, Chancellor Strine cut the fee requested by plaintiffs' lawyers by 75%. In *Revlon*, Vice Chancellor Laster took a case away from lead counsel entirely, presumably dashing their fee hopes as well. Unsurprisingly, fees are an important factor in lawyers' choice of where to file suit.[108] Our interviewees told us that Delaware courts scrutinize fee requests closely, but elsewhere judges routinely approve fee awards, at least if the defendant does not object. A 2011 ruling by Vice Chancellor Laster in a case where shareholder lawsuits had been launched in both Florida and Delaware confirms the point, as he acknowledged that plaintiffs' lawyers, aware that Delaware courts would likely only award attorneys' fees of "$400,000 or $500,000" for the case, could reason "let's go to Florida and get $1 million."[109]

While Delaware courts now scrutinize fee petitions closely, this is a relatively recent development. In most states, courts used a "lodestar" approach where fee awards were based on hours devoted to a case. Delaware courts, in contrast, used the relief obtained as the primary benchmark.[110] Delaware's approach was widely believed to be more generous.[111] As a 1989 law review article said, "the multimillion dollar fees awarded in many shareholder actions brought in Delaware give some credence to an old Italian proverb that describes a lawsuit as a fruit tree in the garden of the lawyer."[112]

Empirical studies of settlements in class actions and derivative suits indicated that the Delaware Court of Chancery approved virtually all settlements parties had reached and endorsed the awarding of the full amount of attorneys' fees agreed

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106. Joseph W. Bishop, Jr., *Sitting Ducks and Decoy Ducks: New Trends in the Indemnification of Corporate Directors and Officers*, 77 YALE L.J. 1078, 1084 (1968).

107. Branson (1990), *supra* note 27, at 91.

108. COMMITTEE ON SECURITIES LITIGATION (2010), *supra* note 68, at 5; Todd J. Zywicki, *Is Forum Shopping Corrupting America's Bankruptcy Courts?*, 94 GEO. L.J. 1141, 1174 (2006); *see also* Coffee (1986), *supra* note 71, at 686 (noting that in representative litigation, the attorney's recovery, rather than expected plaintiffs' damages, create the incentive to sue).

109. Status Conference at *9, *In re* Burger King Holdings, Inc., S'holders Litig., C.A. No. 5808–VCL (Del. Ch. Jan. 19, 2011).

110. Macey & Miller (1987), *supra* note 25, at 497.

111. Branson (1990), *supra* note 27, at 101–02.

112. Donald E. Pease, *Delaware's Disclosure Rule: The "Complete Candor" Standard, Its Application, and Why Sue in Delaware*, 14 DEL. J. CORP. L. 445, 496–97 (1989).

upon in pretty much all instances.[113] Delaware courts accordingly gained a reputation for being plaintiff friendly in shareholder litigation.[114] This, moreover, was perceived by Delaware judges to be part of the Delaware brand. Then Vice Chancellor Carolyn Berger co-authored an empirical study of attorneys' fees awards from 1990 to 1992 and said of the study, "we have come up with some internal statistics that just might demonstrate convincingly why plaintiffs' lawyers often head in our direction."[115] Her summary: "Plaintiffs stand an extremely good chance of having their settlements approved here, and their lawyers are likely to be awarded handsome fees."[116]

Chancellor Chandler, in a 1999 case, defended Delaware's approach, saying the judiciary wanted to ensure plaintiffs' lawyers were "economically incentivized to perform [a] service on behalf of shareholders."[117] A change of heart was imminent, however. Chancellor Chandler, in a 2001 working paper that updated Vice Chancellor Berger's study and confirmed that Delaware judges typically approved attorney fee proposals, indicated his unease, saying that "in the absence of an adversarial process at the fee award stage, judges in a common law system do not have the tools necessary to make consistently reasonable and fair judgments about such questions."[118]

Chancellor Chandler's misgivings found expression in a 2001 decision. The Grant & Eisenhofer law firm sought approval for a $24.75 million fee in an M&A case where the firm secured a $180 million settlement for minority shareholders in Digex.[119] Chancellor Chandler instead awarded $12.3 million, saying: "There is no reason for the court to believe that a 7.5 percent fee will provide a disincentive to plaintiffs' attorneys or their clients."[120] Grant & Eisenhofer, unsurprisingly, had a different view.[121]

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113. Carolyn Berger & Darla Pomeroy, *Settlement Fever: How a Delaware Court Tackles Its Cases*, BUS. L. TODAY, Sept.–Oct. 1992, at 7 (studying 98 corporate and class action suits arising between 1990 and 1992, where "more than 95 percent of all the proposed settlements were approved . . . and approximately two-thirds of the attorneys' fee [applications] were granted in full"); William B. Chandler III, Awarding Counsel Fees in Class and Derivative Litigation in the Delaware Court of Chancery (Apr. 20, 2001) (unpublished working paper) (on file with the authors) (for settlements between 1998 and 2001, two-thirds of fee petitions were granted in full and the remaining one-third were reduced, on average, by 20%); Elliott J. Weiss & Lawrence J. White, *File Early, Then Free Ride: How Delaware Law (Mis)Shapes Shareholder Class Actions*, 57 VAND. L. REV. 1797, 1847, 1872 (2004) (reporting that all 47 settlements arising from 1999–2001 merger cases were approved, with fees awarded in full in 40 cases).

114. Fisch (2000), *supra* note 2, at 1092.

115. Berger & Pomeroy (1992), *supra* note 113, at 7.

116. *Id.*

117. *In re* Fuqua Indus., Inc. S'holder Litig., 752 A.2d 126, 133 (Del. Ch. 1999).

118. Chandler (2001), *supra* note 113, at 5.

119. David Marcus, *Half a Loaf Is Still Plenty of Bread*, DEL. L. WKLY., May 29, 2001, at 4; *see also* Robert B. Thompson & Randall S. Thomas, *The Public and Private Faces of Derivative Lawsuits*, 57 VAND. L. REV. 1747, 1777–78 (2004) (reporting the *Digex* settlement amount as $165 million).

120. Marcus (2001), *supra* note 119.

121. *Id.*

Other fee-cut cases followed. One was *Cox Communications*.[122] Another was a 2005 ruling by Vice Chancellor Lamb in a takeover case, where he reduced a $1,623,000 proposed award to $450,000.[123] These cases prompted speculation that fee reductions by Delaware judges could encourage lawyers to file elsewhere.[124] Delaware courts nevertheless remain prepared to subject attorneys' fees to "rigorous scrutiny."[125] For instance, in 2010 Vice Chancellor Parsons rejected in *Cox Radio* a $3.6 million fee request and awarded only $1,077,038,[126] and Vice Chancellor Laster, in *Brinckerhoff v. Texas Eastern Products Pipeline Company*, awarded a fee of $10 million rather than the $19.5 million requested despite "significant litigation efforts" because much litigation remained, including expert discovery and trial preparation.[127]

Might the fee cut in the Digex litigation have marked an important turning point? Our data suggests that it might, in that the out-of-Delaware trend for leveraged buyout cases lines up decently with the timing of the *Digex* ruling (see Figure 8). The substantive law relating to leveraged buyouts likely did not play a role, as Delaware judges have long been thought of as being tough on the self-dealing that can occur in these transactions.[128] Might *Cox Communications* have marked a further turning point for the out-of-Delaware trend? Some of our interviewees thought so,[129] but the evidence is mixed. Much of our data suggest a trend that began earlier, around 2000 or 2001, which coincides with *Digex*.

E. Selection of Lead Counsel

The approach the Delaware courts adopt when selecting lead counsel could be an additional cause of the out-of-Delaware trend. A change in approach by Delaware judges, starting in 2000, likely encouraged some plaintiffs' firms to file suits outside Delaware.

Often, multiple lawsuits based on the same facts are filed in the same jurisdiction.[130] The courts in that jurisdiction normally consolidate these suits into a single suit and appoint lead counsel, who will do most of the work and receive most of any eventual fee award.[131] Thus, lead counsel is a coveted position.

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122. *In re* Cox Commc'ns, Inc. S'holders Litig., 879 A.2d 604 (Del. Ch. 2005).

123. *In re* Instinet Grp., Inc. S'holders Litig., No. Civ.A. 1289–N., 2005 WL 3501708, at *1 (Del. Ch. Dec. 14, 2005).

124. Marcus (2006), *supra* note 94.

125. *In re* Cox Radio, Inc. S'holders Litig., C.A. No. 4461–VCP, 2010 WL 1806616, at *20 (Del. Ch. May 6, 2010).

126. *Id.* at *23.

127. Brinckerhoff v. Texas E. Prods. Pipeline Co., 986 A.2d 370, 396 (Del. Ch. 2010).

128. *See, e.g.*, Rock (1997), *supra* note 86.

129. *See also* Micheletti & Parker (2012), *supra* note 10, at 8–9 ("[S]ome track the origin of the multi-jurisdictional boom to . . . *Cox*").

130. For our large M&A transaction dataset, in cases where at least one lawsuit was filed Delaware targets received an average of 6.3 lawsuits per deal before consolidation of multiple filings in the same jurisdiction. The equivalent figure for LBOs was 3.2.

131. Thompson & Thomas (2004), *supra* note 48, at 156 n.94; Jill E. Fisch, *Lawyers on the Auction Block: Evaluating the Selection of Class Counsel by Auction*, 102 COLUM. L. REV. 650, 654 (2002).

If courts resolve disputes concerning lead counsel status by focusing on which law firm was first to file, a "filing Olympics" is a logical by-product. A bias in favor of the first law firm to file used to apply in Delaware corporate litigation, and often continues to apply elsewhere. However, beginning in 2000, the Delaware courts moved to an approach closer to that used in federal securities cases, giving preference to firms whose clients had a substantial economic stake in the outcome.[132] More recently, Delaware courts have also focused on the reputation and past results of law firms seeking the lead counsel role.[133] Law firms with a limited track record or lacking a client with a large shareholding thus have had reason to file elsewhere.

Traditionally, the Delaware courts took a hands-off approach in determining who should be lead counsel, and expected plaintiffs' lawyers to sort this out for themselves.[134] The plaintiffs' bar responded with a simple organizing principle: the firm who filed first should be lead or co-lead counsel. The natural result was "a race to the courthouse."[135] Thompson and Thomas report that of 623 deal-related corporate law class actions filed in Delaware in 1999 and 2000, almost 70% were filed within three days of the announcement of the transaction.[136]

The Delaware Supreme Court acknowledged in 1993 that the "'first to file' custom" had generated "a plethora of superficial complaints."[137] Only in 2000, however, did the Delaware courts directly question the presumption that prompt filing would be rewarded if disputes arose among plaintiffs' lawyers over the lead counsel role. In *TCW Technology Ltd. Partnership v. Intermedia Communications, Inc.*,[138] which arose from the same Digex transaction that prompted Chancellor Chandler's ruling on attorneys' fees, he said, "Although it might be thought, based on myths, fables, or mere urban legends, that the first to file a lawsuit in this Court wins some advantage in the race to represent the shareholder class, that assumption, in my opinion, has neither empirical nor logical support."[139] The first-to-file "custom" had remained undisturbed because the Delaware courts had left it to plaintiffs' lawyers to sort the matter out for themselves. To quote Chancellor Chandler again:

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132. We discuss the changes in Delaware's approach to appointing lead counsel below. *See infra* note 141 and accompanying text.

133. *See infra* note 145 and accompanying text.

134. Weiss & White (2004), *supra* note 113, at 1846; TCW Tech. Ltd. P'ship v. Intermedia Commc'ns, Inc., No. 18336, 18289, 18293, 2000 WL 1654504, at *3 (Del. Ch. Oct. 17, 2000); *In re* Siliconix Inc. S'holders Litig., No. C.A. 18700–NC, 2001 WL 618210, at *1 (Del. Ch. May 25, 2001).

135. Jill E. Fisch, *Aggregation, Auctions, and Other Developments in the Selection of Lead Counsel Under the PSLRA*, 64 LAW & CONTEMP. PROBS. 53 (2001).

136. Thompson & Thomas (2004), *supra* note 48, at 182–83; *see also* Weiss & White (2004), *supra* note 113, at 1827 (of 104 mergers of Delaware-incorporated public companies occurring between 1999 and 2001, with 77 the initial filing occurred within one day of the merger announcement).

137. Rales v. Blasband, 634 A.2d 927, 935 n.10 (Del. 1993).

138. *TCW Tech. Ltd. P'ship*, 2000 WL 1654504.

139. *Id.* at *3.

> Over the past ten years, members of the Court of Chancery have been asked, with increasing frequency, to become involved in the sometimes unseemly internecine struggles within the plaintiffs' bar over the power to control, direct and (one suspects) ultimately settle shareholder lawsuits filed in this jurisdiction. In every single instance that I am able to recall, this Court has resisted being drawn into such disputes. In every instance, the plaintiffs' bar has been able to work out a consolidation compromise. It may have been imperfect, but the compromise has always seemed, in the end, to accommodate reasonably the interests of all the parties and the Court.[140]

With plaintiff self-regulation having failed in the Digex litigation, Chancellor Chandler named as lead counsel Grant & Eisenhofer, the firm acting on behalf of an institutional shareholder, the Kansas Public Employees Retirement System. He identified three factors a Delaware court would consider should the issue arise again: the quality of the pleadings, the energy and enthusiasm demonstrated by the various attorneys, and the size of the economic stake each plaintiff had in the litigation.[141] This third factor, as Chancellor Chandler noted, was similar to the approach adopted in the Private Securities Litigation Reform Act of 1995 (PSLRA)[142] for securities class actions.[143] Chancellor Chandler did not formally adopt the federal model, but he did say it was appropriate "to give recognition to large shareholders or significant institutional investors who are willing to litigate vigorously on behalf of an entire class of shareholders."[144] Recent Delaware Court of Chancery decisions involving a leadership fight suggest that attorneys' credentials will also be important.[145]

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140. *Id.*

141. *Id.* at *4; *see also In re* Siliconix Inc. S'holders Litig., No. C.A. 18700–NC, 2001 WL 618210, at *2 (Del. Ch. May 25, 2001) (identifying the same factors and noting possible additional relevant factors).

142. Pub. L. No. 104-67, 109 Stat. 737.

143. *See TCW Tech. Ltd. P'ship*, 2000 WL 1654504, at * 4.

144. *Id.* Delaware courts subsequently indicated that the size of a plaintiff's holding was not to be "used to generate a formalistic ranking, . . . but rather" was relevant in determining whether the plaintiff had "an economic incentive to monitor counsel." *In re* Revlon, Inc. S'holders Litig., 990 A.2d 940, 955 (Del. Ch. 2010); *see also* Wiehl v. Eon Labs, No. Civ.A. 1116–N, 2005 WL 696764, at *3 (Del. Ch. Mar. 22, 2005).

145. *See* Transcript of Plaintiffs' Motion for a Preliminary Injunction & the Court's Ruling at *6, *In re* Compellent Tech., Inc. S'holder Litig., C.A. No. 6084–VCL (Del. Ch. Jan. 13, 2011) (Vice Chancellor Laster said that "the key factor for me . . . is what your [firm's] track record in generating tangible benefits for stockholders."); *In re* Del Monte Foods Co. S'holder Litig., No. 6027–VCL, 2010 Del. Ch. LEXIS 255, at *17–18, 27–34 (Del. Ch. Dec. 31, 2010) (Vice Chancellor Laster granted lead counsel status to a law firm's attorneys representing a pension fund owning far fewer shares than another contender, based on the capabilities of the law firms involved); Transcript of Oral Argument on Plaintiffs' Motions to Consolidate and to Appoint Lead Plaintiff and Co-Lead Counsel at 33, *In re* Novell Inc. S'holder Litig., No. 6032–VCN, 2011 WL 4091502 (Del. Ch. Dec. 17, 2010) (Vice Chancellor Noble appointed lead counsel based on his determination of which law firm would be most likely to produce a favorable outcome for shareholders).

The Delaware courts did not entirely abandon the first-to-file custom after *TCW Technology*. In *In re IBP, Inc., Shareholders Litigation*, a 2001 case where Chancellor Strine declined to stay a Delaware suit in favor of the Arkansas court system, he said:

> The fact that the court treats these actions as contemporaneously filed does not mean that the first time-stamp should lose all relevance. In close cases where the issue of convenience is in equipoise, it makes sense as a matter of comity to regard the first time-stamp factor as a tipping one in a *forum non conveniens* analysis.[146]

Subsequent cases would soon establish, however, that any first-to-file edge was weak at best in Delaware courts.

In the 2003 case of *Biondi v. Scrushy*, Vice Chancellor Strine declined to stay a Delaware derivative lawsuit in deference to litigation launched earlier in Alabama. In so doing, he remarked on the "public policy interest favoring the submission of thoughtful, well-researched complaints – rather than ones regurgitating the morning's financial press" and observed that "Delaware law places more emphasis on quality than speed when assessing derivative complaints."[147] Similarly, in *Rosen v. Wind River Systems*, a 2009 case where Vice Chancellor Parsons declined to dismiss a Delaware suit in deference to suits filed earlier in California, he declined to "reward the most fleet-of-foot in a sprint to the courthouse."[148]

A 2010 case, *King v. VeriFone Holdings*, confirms that being first to file is of limited value in Delaware. The case involved an application to examine corporate books and records under Delaware corporate law by an applicant who was already lead plaintiff in a derivative suit in federal court arising from the same facts. Vice Chancellor Strine rejected the application, saying he preferred not to reward "plaintiffs and their counsel who sue first, and investigate and think second."[149] The Delaware Supreme Court reversed this ruling but noted that "[b]eing the 'first to file' does not automatically confer lead-plaintiff status."[150]

Although disfavored in Delaware, the first-to-file "custom" has retained vibrancy elsewhere. When plaintiffs' lawyers cannot resolve for themselves who should be lead counsel, judges outside Delaware often appoint as lead or co-lead counsel the firm that filed first.[151] *King v. VeriFone Holdings* illustrates the vitality of the first-to-file custom outside Delaware. Counsel for the lead plaintiff in the

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146. *In re* IBP, Inc., S'holders Litig. v. Tyson Foods, Inc., No. CIV.A.18373, 2001 WL 406292, at *8 (Del. Ch. Apr. 18, 2001).

147. Biondi v. Scrushy, 820 A.2d 1148, 1162 (Del. Ch. 2003).

148. Rosen v. Wind River Sys., Inc., C.A. No. 4674–VCP, 2009 WL 1856460, at *5 (Del. Ch. June 26, 2009).

149. King v. VeriFone Holdings Inc., 994 A.2d 354, 364 n.34 (Del. Ch. 2010) *rev'd*, 12 A.3d 1140 (Del. 2011).

150. King v. VeriFone Holdings Inc., 12 A.3d 1140, 1151 (Del. 2011).

151. ALBA CONTE & HERBERT B. NEWBERG, NEWBERG ON CLASS ACTIONS § 9.35 (4th ed. 2002); Lebovitch, Silk & Friedman (2011), *supra* note 78, at 3; Quinn (2011), *supra* note 10, at 22. No statute or procedural rule directly gives the courts authority to appoint lead counsel, but *MacAlister v. Guterma*, 263 F.2d 65 (2d Cir. 1958), is commonly cited as supporting this power. Fisch (2001), *supra* note 135, at 56 n.17.

federal derivative suit admitted in the Delaware hearing that he had filed rapidly in federal court to gain an edge in what Vice Chancellor Strine labeled the "lead counsel Olympics race."[152] As Strine said, "Counsel's sense of the incentive system at work was vindicated." [153]

The more favorable treatment of nimble filers outside Delaware creates incentives for some plaintiffs' lawyers to file outside Delaware. Imagine a modest-sized plaintiffs' firm located in a public company's home state, representing a small stockholder and lacking a strong Delaware track record. The firm is unlikely to garner lead counsel status in Delaware, but it has a chance if it is first to file elsewhere. Moreover, if a more thoughtful complaint is later filed in Delaware, the first-to-file firm can piggyback on the work by Delaware counsel in his own action.

To the extent that *TCW Technology* and related cases encouraged nimble, modest-sized law firms to file cases outside Delaware, the resulting out-of-Delaware trend would have emerged during the first half of the 2000s, consistent with the empirical evidence summarized in Part II.[154] One should not assume, however, that fast filing has ceased in Delaware. As Vice Chancellor Laster observed in 2010, "[T]he first cases often appear minutes or hours after the announcement with others following within a matter of days."[155] Presumably, the fast filers believe that filing first continues to be advantageous, perhaps in private negotiations over the lead counsel role with other firms.

The first-to-file presumption is not absolute outside Delaware. According to *Newberg on Class Actions*: "The first attorney to file is not entitled to special consideration for appointment as lead counsel . . . . "[156] Moreover, the federal courts, in assigning lead counsel in a corporate case, will likely be influenced by the securities law presumption in favor of the law firm with the largest client.[157] Still, a likely partial cause of the out-of-Delaware trend is the fact that filing first can help in a lead counsel contest and, since *TCW Technology*, likely helps more outside Delaware.

F. Changes to Federal Securities Law and "Tagalong" Derivative Suits

In the 1980s, federal securities class actions burgeoned, particularly against high-tech companies.[158] A backlash ensued,[159] which led to the adoption of the

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152. King v. VeriFone Holdings, Inc., 994 A.2d 354, 357 (Del. Ch. 2010), *rev'd*, 12 A.3d 1140 (Del. 2011).

153. King v. VeriFone Holdings, Inc., 994 A.2d at 358.

154. Caution is required in inferring causation. The decision in *TCW Technology* did not elicit much press attention. The only article discussing the case we found was a brief one that did not discuss the out-of-Delaware incentives the decision created: *Del. Judge Uses Reform Act Model, Chooses Institutional Investor for Lead Role*, ANDREWS DEL. CORP. LITIG. REP., Nov. 13, 2000, at 3.

155. *In re* Revlon, Inc. S'holders Litig., 990 A.2d 940, 943 (Del. Ch. 2010); *see also In re* Cox Commc'ns, Inc. S'holder Litig., 879 A.2d 604 (Del. Ch. 2005).

156. CONTE & NEWBERG (2002), *supra* note 151, § 9.35.

157. See discussion of case law in King v. VeriFone Holdings, Inc., 12 A.3d 1140, 1151 n.66 (Del. 2011).

158. Roberta Romano, *The Shareholder Suit: Litigation Without Foundation?*, 7 J.L.

PSLRA in 1995 and the Securities Litigation Uniform Standards Act (SLUSA) in 1998.[160] Prior to the PSLRA, one did not normally see securities class actions and derivative suits both filed based on the same underlying facts.[161] However, the limits that the PSLRA imposed on discovery changed this, and generated a surge in "parallel" or "tagalong" derivative suits launched in state court in parallel with federal securities claims and arising from similar facts.[162] For reasons we discuss below, many of these derivative suits are filed outside Delaware.

The PSLRA responded, in part, to a belief that plaintiffs' lawyers often filed securities class actions with weak facts and then used discovery to conduct a "fishing expedition" for facts that would support their claims, while counting on the high cost of discovery, borne largely by defendants, to create leverage to settle even weak cases.[163] The PSLRA therefore required securities lawsuits to be supported by a detailed factual pleading and barred discovery until a case survived a motion to dismiss.[164] To survive that motion, a complaint had to allege with particularity facts giving rise to a strong inference that the defendants had acted with scienter.[165]

Many plaintiffs' lawyers initially sidestepped the PSLRA by bringing securities suits in state court.[166] Congress reacted by enacting SLUSA in 1998, which let defendants remove a securities class action lawsuit filed in state court to federal court.[167] State securities class actions quickly disappeared.[168]

ECON. & ORG. 55, 58–60 (1991); *Securities Fraud Litigation: Both Sides Agree It Is a Never-Ending Battle*, CORP. LEGAL TIMES, Sept. 1992, at 1 (remarks of William Lerach, indicating that the number of securities class action rose steadily from 1982 to 1991); Nanette L. Stasko, *Competitive Bidding in the Courthouse: In re Oracle Securities Litigation*, 59 BROOK. L. REV. 1667, 1670–71 (1994).

159. William S. Lerach, *Securities Class Actions and Derivative Litigation Involving Public Companies: One Plaintiff's Perspective*, *in* 399 PRACTISING LAW INSTITUTE, LITIGATION AND ADMINISTRATIVE PRACTICE COURSE HANDBOOK SERIES 65, 99–107 (1990).

160. The PSLRA is Pub. L. No. 104-67, 109 Stat. 737 (codified in various parts of 15 U.S.C.). The SLUSA is Pub. L. No. 105-353, 112 Stat. 3227 (codified at 15 U.S.C. § 77p(b) and 15 U.S.C. § 78bb).

161. *See* Jessica Erickson, *Corporate Misconduct and the Perfect Storm of Shareholder Litigation*, 84 NOTRE DAME L. REV. 75, 78 (2008); David Priebe, *Piling On: The Reemergence of the Parallel Derivative Lawsuit as the Federal Securities Class Action Window Closes*, *in* 1136 PRACTISING LAW INSTITUTE, CORPORATE LAW AND PRACTICE COURSE HANDBOOK SERIES 333, 335 (1999); Robert B. Thompson & Randall S. Thomas, *The Public and Private Faces of Derivative Lawsuits*, 57 VAND. L. REV. 1747, 1773 (2004) (indicating that where plaintiffs could bring a federal securities class action or a derivative lawsuit under Delaware corporate law, they would usually opt for the former).

162. *See* Erickson (2010), *supra* note 10, at 1778; Erickson (2008), *supra* note 161, at 85–86; Priebe (1999), *supra* note 161, at 337, 339.

163. Erickson (2008), *supra* note 161, at 93.

164. *See* 15 U.S.C. §§ 77z-1(b), 78u-4(b)(3)(B) (2006).

165. *See id.* (discovery); *id.* § 78u-4(b)(2) (pleading standard).

166. Peter Q. Bassett & Kelly C. Wilcove, *Post Reform Act Developments in Derivative, Financial Advisor, and State Court Securities Litigation*, *in* 1199 PRACTISING LAW INSTITUTE, CORPORATE LAW AND PRACTICE COURSE HANDBOOK SERIES 545, 550–51 (2000); Jordan A. Costa, Note, *Removal of Securities Act of 1933 Claims After SLUSA: What Congress Changed, and What It Left Alone*, 78 ST. JOHN'S L. REV. 1193, 1202–03 (2004).

167. 15 U.S.C. §§ 77p(c), 78bb(f)(2).

168. Priebe (1999), *supra* note 161, at 335; Costa (2004), *supra* note 166, at 1205.

Plaintiffs' lawyers then changed tactics again. Many began to file "parallel" or "tagalong" derivative suits under state corporate law based on the same basic facts as a securities case.[169] There is considerable potential for derivative suits to complement or substitute for securities suits because director or officer misconduct that results in misleading or incomplete disclosure can provide the foundation for both types of claims.[170] Plaintiffs' lawyers who had launched securities class actions found it useful to file parallel derivative suits because they could use discovery in the corporate case to provide the detailed factual support needed for the federal securities claim.[171] The derivative case might also contribute to settlement value. Another possibility was for a firm that did not have a lead role in a securities class action to launch a parallel derivative suit, perhaps seeking to get a piece of an expected overall global settlement of both cases.[172]

SLUSA did not allow defendants to remove derivative suits filed in state courts to federal court because it contained a "Delaware carve-out" that exempted actions under state corporate law.[173] Moreover, state courts generally rejected defense petitions to stay discovery in a derivative suit until after the federal motion to dismiss in the accompanying securities litigation was decided.[174] The overall result was what one press report termed an "explosion" in tagalong derivative lawsuits.[175] One study reports that the fraction of settled securities class actions accompanied by a parallel derivative suit ranged from only 11% to 26% annually between 1997

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169. *See* Erickson (2010), *supra* note 10, at 1776; Priebe (1999), *supra* note 161, at 335.

170. *See* Malone v. Brincat, 722 A.2d 5 (Del. 1998); Erickson (2008), *supra* note 159, at 88–90 (2008). Often, the alleged misconduct is by executives, who do not benefit from a section 102(b)(7) charter provision barring monetary recovery from directors for good faith conduct. These provisions do not protect officer-directors when they act in their officer capacity. Lyman P.Q. Johnson, *Corporate Officers and the Business Judgement Rule*, 60 BUS. LAW. 439, 461 (2005). Plaintiffs often allege that the directors knowingly participated or acquiesced in dishonest conduct so as to justify not making demand on the board to bring a derivative suit. *See* Priebe (1999), *supra* note 161, at 337, 339.

171. Michael A. Collora & David M. Osborne, *Class-Action Reforms Spur Derivative Claims*, NAT'L L.J., Feb. 15, 1999, at B8; Erickson (2008), *supra* note 161, at 94; *Lower Court Ruling Will Encourage 'Tag Along' Derivative Suits, Say Directors*, ANDREWS SEC. LITIG. & REG. REP., Apr. 14, 1999, at 5.

172. *See Derivative Suits*, ORRICK.COM, http://www.orrick.com/practices/securities_litigation/derivative_suits.asp.

173. 15 U.S.C. §§ 77p(d)(1), 77p(f)(2)(B), 78bb(f)(3), 78bb(f)(5)(C) (2006); Bassett & Wilcove (2000), *supra* note 166, at 557–58.

174. For a summary of relevant decisions, see Marvin L. Frank, *Staying Derivative Actions Pursuant to PSLRA and SLUSA*, N.Y. L.J., Oct. 21, 2005, at 4. There have been some cases, however, where courts have stayed "piggyback" derivative actions. *See, e.g.*, Breault v. Folino, No. SACV010826GLTANX, 2002 WL 31974381 (C.D. Cal. Mar. 15, 2002); Brudno v. Wise, No. Civ.A. 19953, 2003 WL 1874750 (Del. Ch. Apr. 1, 2003).

175. Mark Friedman, *Dillard's Inc. Shareholders Try New Tack*, ARK. BUS., July 6, 2009, at 1; *see also* Frank (2005), *supra* note 174.

and 2002 but then grew to 65% in 2007 and has remained above 50% annually thereafter.[176]

Due to features of Delaware law, the PSLRA-induced surge in derivative litigation likely contributed to the out-of-Delaware corporate litigation trend. Many states permit discovery in derivative actions prior to a motion to dismiss; Delaware is among the minority that do not.[177] Many states also routinely allow expedited discovery; in contrast, the Delaware courts are selective in granting expedited discovery requests, and often deny them unless there is a colorable claim of irreparable harm, which does not exist in most tagalong cases.[178] Our interviewees also advised us that when the Delaware courts do grant expedited discovery, it sometimes comes too late to be useful in seeking an injunction. This is a particular concern in takeover cases. Plaintiffs' attorneys who bring tagalong derivative suits usually want early discovery, so they have a strong incentive to proceed outside Delaware. The post-SLUSA emergence of tagalong derivative suits coincided in time with the out-of-Delaware trend, and plausibly contributed to the trend.

Delaware corporate law offers a potential substitute for expedited discovery—inspection of books and records under section 220 of the Delaware General Corporation Law. Plaintiffs can seek to use information gained through this inspection to support their claims in a derivative suit or a securities action.[179] However, a section 220 application is costly and risky, as considerable effort is typically needed to succeed. Moreover, expedited court handling of a section 220 application, or of discovery if the application is granted, is not assured. In addition, even if a section 220 application is granted and the plaintiffs secure additional evidence from the inspection of books and records and then launch a derivative suit, the Delaware courts may order a stay of the derivative suit if it overlaps too closely with a related securities lawsuit.[180] Thus, while some plaintiffs' lawyers have brought section 220 applications instead of tagalong derivative suits, many have found it easier to file outside Delaware and pursue conventional expedited discovery.

G. Summary

Delaware is well known as a manager-friendly state. One source for the out-of-Delaware trend would be if Delaware had become even more so beginning around 2000, thus driving plaintiffs' lawyers to file cases elsewhere. We cannot rule out this explanation as part of the overall story. Still, on the whole, the Delaware courts do not appear to be significantly more pro-manager today than in the 1990s. The dominant explanations for the out-of-Delaware trend lie elsewhere.

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176. JORDAN MILEV, ROBERT PATTON, SVETLANA STARYKH & JOHN MONTGOMERY, RECENT TRENDS IN SECURITIES CLASS ACTION LITIGATION: 2011 YEAR-END REVIEW 16 (2011), *available at* http://www.nera.com/67_7557.htm.

177. *See* Frank (2005), *supra* note 174.

178. *Id.* (discussing eight leading cases where the issue arose).

179. Radin (2006), *supra* note 3, at 1290, 1296; *see also* Romero v. Career Educ. Corp., No. Civ.A. 793–N, 2005 WL 5750613 (Del. Ch. July 19, 2005).

180. Brenner v. Albrecht, C.A. No. 6514–VCP, 2012 WL 252286 (Del. Ch. Jan. 27, 2012).

We have identified four factors that likely contributed to the out-of-Delaware trend: (i) statements by Delaware judges expressing doubts, sometimes strong ones, about the plaintiffs' bar and the suits that they bring; (ii) Delaware judges cutting plaintiffs' lawyers' fee requests; (iii) Delaware courts retreating from the "first to file" custom in choosing lead counsel; and (iv) plaintiffs' lawyers beginning to file tagalong derivative suits, usually outside Delaware because expedited discovery is often easier to obtain elsewhere. Each of these factors directly affects plaintiffs' lawyers, who decide where corporate law cases will be brought. There is no conclusive case for causation. Nevertheless, as we turn to the policy implications of the out-of-Delaware trend and potential responses by Delaware and Delaware-incorporated companies, our departure point is that factors that the Delaware courts and legislators can influence helped to prompt the migration of cases out of Delaware. A change of course thus might bring many cases back.

Our analysis of causes of the out-of-Delaware trend is not exhaustive. Changes to the plaintiffs' bar are also potentially relevant. For instance, Chancellor Strine's explanation for what Ted Mirvis termed the "Anywhere But Chancery" phenomenon was that there had been "a fragmentation in the plaintiffs' bar . . . that has caused there to be more of a melee."[181] The enactment of the PSLRA, with its emphasis on detailed factual pleadings and its presumption that the lead counsel role should be assigned to the law firm with the largest client based on shares held, drove many smaller, less well-capitalized firms out of the securities fraud area, and some of these firms shifted to corporate litigation.[182] In addition, during the mid-2000s various large plaintiff firms who had focused primarily on securities litigation began to put greater emphasis on corporate suits, with potentially lucrative options backdating cases being particularly alluring.[183] Greater competition among plaintiffs' lawyers in the corporate law area could have contributed to the out-of-Delaware trend because, for some firms, filing outside Delaware could provide an escape from a filing logjam in Delaware. We do not pursue this factor further here because from a policy perspective Delaware is not in a position to reverse the plaintiffs' bar's recent fragmentation, but do so in related research.[184]

IV. THE DELAWARE COURTS' BALANCING ACT

Losing litigation market share to other courts puts Delaware judges on the spot. The trend, if sustained, could erode their status as the de facto "national" corporate judiciary, as well as the value of Delaware's body of precedents. Thus, Delaware

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181. Quoted in *Anywhere but Chancery* (2007), *supra* note 1, at 18.

182. *See* Stevelman (2009), *supra* note 10, at 99; Renee Deger, *State of Alert: Silicone Valley Corporate Firms on Guard as the Plaintiffs Bar Takes Securities Cases to State Court*, RECORDER (S.F.), Aug. 9, 2001, at 3.

183. Justin Scheck, *Class Rules Not So Bad After All*, RECORDER (S.F.), July 3, 2006; Susanne Sclafane, *Plaintiffs Choosy About Derivative Suit Filings, Lawyer Tells D&O Underwriters*, NAT'L UNDERWRITER PROP. & CASUALTY, Mar. 1, 2010.

184. John Armour, Bernard S. Black & Brian Cheffins, *Delaware Corporate Litigation and the Fragmentation of the Plaintiffs' Bar*, 2012 COL. BUS. L. REV. (forthcoming 2012), *available at* http://ssrn.com/abstract=2030398.

judges have incentives to address the out-of-Delaware trend, but to succeed they will need to execute a delicate balancing act. We discuss in this section these incentives, together with the opportunities Delaware judges have to reverse the trend and the constraints they face if they try.

A. Judicial Incentives to Reverse the Out-of-Delaware Trend

Delaware's Court of Chancery judges are often characterized as an elite judicial corps that engages in principled lawmaking, thus enhancing Delaware's legitimacy as a standard-setter for corporate law.[185] The state's judges "take pride in keeping up with business trends" and responding quickly and professionally to new challenges.[186] Former Chancellor William Allen maintained in a 2000 speech that "pride in the tradition of excellence and the importance that Delaware law has played nationally act as an important non-economic incentive for judges who serve under the light of national publicity to work hard and do their best."[187] A Delaware Chancery Court judge was quoted anonymously in a 2002 law review article as saying Delaware judges are "driven by 'pride and service,'" and "'we believe that we are doing something that ben efits all of society, and that it is important to do this well.'"[188] Similarly, Vice Chancellor Laster drew attention in a 2011 ruling to the Delaware courts' expertise in corporate law and their corresponding "comparative advantage" in resolving corporate suits.[189] The elite status of Delaware judges, however, depends on their having a steady flow of cases to resolve, particularly those that could generate important precedents or affect major transactions. The out-of-Delaware trend puts that flow under threat and gives Delaware's judges an incentive to seek to channel cases back to Delaware.

Concerns about the Delaware bar provide the state's judiciary with a second reason to try to regain case flow. As Part II has shown, the raw number of cases filed in Delaware has not dropped despite Delaware's loss of litigation market share. Instead, the erosion of Delaware's market share has been roughly offset by a greater total number of suits. Still, Delaware corporate litigators surely prefer not to lose market share, and Delaware judges may be receptive to such concerns.[190]

Potential tarnishing of the value of Delaware incorporation gives Delaware judges a third reason to protect their "turf." Extensive precedent, created and interpreted by expert judges, is part of what Delaware "sells."[191] As a 2001 article

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185. *See, e.g.*, Kahan & Rock (2005), *supra* note 11, at 1602–04, 1611; Simmons (2008), *supra* note 17, at 1142–43.

186. Roe (2003), *supra* note 11, at 594.

187. William T. Allen, *The Pride and the Hope of Delaware Corporate Law: Keynote Address by the Honorable William T. Allen*, 25 DEL. J. CORP. L. 70, 73 (2000).

188. Marcus Cole, *"Delaware Is Not a State": Are We Witnessing Jurisdictional Competition in Bankruptcy?*, 55 VAND. L. REV. 1845, 1875 (2002).

189. Transcript of Plaintiffs' Motion for a Preliminary Injunction & the Court's Ruling at *15, *In re* Compellent Tech., Inc. S'holder Litig., C.A. No. 6084–VCL (Del. Ch. Jan. 13, 2011).

190. *Cf.* Macey & Miller (1987), *supra* note 25, at 500 (indicating that Delaware judges may be responsive to interest groups but to a lesser extent than legislators).

191. *Supra* notes 20–22 and accompanying text.

entitled "Incorporate in Delaware? Yes" put it: "[T]he inability of other states to actually create a judicial system as competent, as predictable, and as quick as Delaware's will always give Corporate America great pause when prodded to incorporate elsewhere."[192] A sustained loss of case flow could diminish Delaware's ability to charge a premium price for incorporations. As Douglas Branson has said of Delaware, "Litigation and the flow of chancery and supreme court opinions thereby produced actually generate the predictability hometown counsel and their corporate manager clients desire."[193]

Mergers between public companies, going private transactions, and bankruptcies steadily deplete the number of Delaware public companies, so Delaware needs a steady flow of new incorporations to maintain its status as the primary home for U.S. public companies.[194] If Delaware's attractiveness as a venue for incorporation diminishes, Nevada, Delaware's closest (albeit distant) rival in the market for out-of-state incorporations,[195] might become more popular. So might incorporating locally. The Delaware judiciary reputedly is sensitive to signals generated by the market for incorporation.[196] Hence, concerns about Delaware's *incorporation* market share could elicit an effort by Delaware's judges to recapture *litigation* market share.

There is no evidence yet that Delaware is losing incorporation business. Among Fortune 500 companies, the proportion incorporated in Delaware in 2010 was 63% as compared with 60% in 2005, and 76% of all 2010 initial public offerings were by Delaware companies.[197] This should not be surprising, given that incorporating in Delaware remains a safe, well-understood choice.

If an out-of-Delaware litigation trend did weaken Delaware's stock of precedents and thereby weakened its dominance in the market for incorporations, Delaware could potentially respond by cutting the price it charges for incorporations. Moreover, while a loss of litigation market share will affect Delaware's ability to generate new precedents, Delaware judges will still retain considerable control over Delaware case law because the Delaware courts have the final say on corporate law doctrine for Delaware companies.[198] Options backdating suits illustrate the influence of Delaware decisions, even if few in number. While

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192. John L. Reed & Frank E. Noyes, *Incorporate in Delaware? Yes*, DIRECTORS & BOARDS, Winter 2001, at 33, 34.

193. Branson (1990), *supra* note 27, at 91.

194. Mark J. Roe, *Delaware's Shrinking Half-Life*, 62 STAN. L. REV. 125, 134, 139–40 (2009).

195. Michal Barzuza & David C. Smith, *What Happens in Nevada? Self-Selecting into Lax Law* (Va. Law & Econ., Research Paper No. 2011-08, 2011), *available at* http://ssrn.com/abstract=1644974.

196. Timothy P. Glynn, *Delaware's Vantagepoint: The Empire Strikes Back in the Post-Post-Enron Era*, 102 NW. U. L. REV. 91, 105 (2008).

197. DEL. DEP'T OF STATE, DIV. OF CORPS., 2010 ANN. REP. 1 (2011), *available at* http://corp.delaware.gov/10CorpAR.pdf; DEL. DEP'T OF STATE, DIV. OF CORPS., 2005 ANN. REP. 1 (2006), *available at* http://corp.delaware.gov/2005%20doc%20ar.pdf.

198. Randy J. Holland, *Delaware's Business Courts: Litigation Leadership*, 34 J. CORP. L. 771, 781 (2009).

plaintiffs' lawyers largely bypassed Delaware when filing these suits,[199] legal commentators analyzing options backdating devoted considerable attention to the few Delaware decisions.[200] Moreover, with takeovers, many cases likely to generate precedents are initiated by bidders rather than shareholders, and defense counsel interviewees advised us that Delaware remains the principal locus for suits by bidders.[201]

While Delaware case law will remain highly influential for Delaware companies even in suits brought outside Delaware, an out-of-Delaware trend could still reduce the value of Delaware incorporation if non-Delaware judges or juries fail to apply Delaware precedents as reliably as Delaware judges.[202] As Kenton King, a litigation partner at Skadden Arps, a leading M&A firm, said in 2006: "What I tell clients is that even though Delaware law is being applied, when it's being applied [outside Delaware], the predictability goes down."[203]

The out-of-Delaware trend could also generate muddled case law that reduces the value of Delaware incorporation. Decisions by non-Delaware courts on Delaware corporate law would not be binding, either on the Delaware courts or on courts anywhere besides the court's home jurisdiction. Nevertheless, such case law might carry weight, especially where there was limited Delaware precedent. How much weight would be anyone's guess, but there remains a risk that fewer Delaware-generated precedents will erode the benefits companies derive from being incorporated in Delaware.

The case law on director good faith illustrates the potential importance of the out-of-Delaware trend for case law precedents. The question of good faith is central for the many Delaware public companies that have section 102(b)(7) charter provisions, which eliminate directors' monetary liability for breach of fiduciary duty for actions taken in good faith. The Delaware courts have ruled that to establish lack of good faith, plaintiffs must show either a conflict of interest or "conscious disregard" of duty.[204] Whether conduct is egregious enough to violate this standard is a recurring issue in corporate suits. As of yet, there is no Delaware

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199. *See supra* note 64 and accompanying text.

200. *See* Ryan v. Gifford, 918 A.2d 341 (Del. Ch. 2007); Desimone v. Barrows, 924 A.2d 908 (Del. Ch. 2007). For commentators focusing on these cases, see Abbott (2009), *supra* note 61, at 604–17; *Corporate Governance*, MONDAQ, Aug. 3, 2007, at 1, *available at* 2007 WLNR 14910004; John L. Reed & Paul D. Brown, *Corporate Governance Litigation: 2007 Review*, DIRECTORS & BOARDS, Summer 2008, at 16.

201. Our interviewees advised that for bidders, the Delaware judges' expertise, ability to act quickly, and lack of "home town bias" are critical factors. While Delaware courts are sometimes reluctant to grant expedited discovery in suits by shareholders, *see supra* note 178 and accompanying text, they do grant it routinely for suits by bidders. *See* MacFadyen (2010), *supra* note 51.

202. *See* Kamar (1998), *supra* note 27, at 1930.

203. Marcus (2006), *supra* note 94. King was a partner in Skadden Arps's Palo Alto office. *Id.*

204. *In re* Walt Disney Co. Derivative Litig., 906 A.2d 27 (Del. 2006); Stone v. Ritter, 911 A.2d 362 (Del. 2006). Conscious disregard of duty is also relevant in assessing whether plaintiffs can be excused, in a derivative case, from making demand on the board of directors to bring the suit itself. *See* Andrew C.W. Lund, *Rethinking* Aronson*: Board Authority and Overdelegation*, 11 U. PA. J. BUS. L. 703, 720–23 (2009).

case in which conscious disregard has been found, meaning there is little Delaware guidance on which fact patterns might meet this standard. The leading cases finding sufficient evidence of conscious disregard to withstand a motion to dismiss or a motion for summary judgment are in fact two federal cases, *Abbott Laboratories* in the Seventh Circuit and *Pfizer* in the Southern District of New York.[205]

In *Pfizer*, the court rejected the defendants' motion to dismiss a derivative suit against the directors of Pfizer, a major pharmaceutical company incorporated in Delaware. The suit alleged that the directors had consciously disregarded evidence of widespread "off-label" drug marketing. Judge Rakoff found that the allegations in the complaint, accepted as true in his ruling on the motion, established a substantial likelihood that the Pfizer directors had deliberately disregarded "red flags" suggesting illegal marketing practices and thus might not be protected by Pfizer's section 102(b)(7) charter provision.[206] It might be some time before the Delaware courts face comparable facts—especially if plaintiffs' lawyers often file "conscious disregard" cases elsewhere.

B. Steps Delaware Judges Could Take to Reverse the Out-of-Delaware Trend

If Delaware judges become concerned with the out-of-Delaware trend, they could take a number of steps to try to reverse it. These fall into two basic categories: modifying the trends that have led plaintiffs' attorneys to file elsewhere and channeling multi-jurisdictional suits toward Delaware by encouraging other courts to defer to Delaware in cases involving Delaware corporate law.

1. Making Delaware a More Plaintiff-Friendly Venue

Delaware courts, if they were inclined to seek to reverse the out-of-Delaware trend, could backtrack on actions that have encouraged plaintiffs' attorneys to file elsewhere. First, given that attorneys' fee cuts may have helped to prompt the out-of-Delaware trend,[207] Delaware courts could move back toward their former fee-friendly posture, at least for cases with significant financial recoveries. As law professor Geoffrey Miller has observed, "Courts cannot engage in commentary if they do not have cases, and attorneys will not bring cases if they do not anticipate a fee."[208] One can see a headline grabbing $300 million fee Chancellor Strine awarded to plaintiffs' attorneys in 2011 in the *Southern Peru* derivative litigation as a strong move in this direction.[209]

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205. *In re* Abbott Labs. Derivative S'holders Litig., 325 F.3d 795 (7th Cir. 2003); *In re* Pfizer Inc. S'holder Derivative Litig., 722 F. Supp. 2d 453 (S.D.N.Y. 2010). One of us (Black) was an expert witness for the plaintiffs in Pfizer.

206. *In re* Pfizer Inc. S'holder Derivative Litig., 722 F. Supp. 2d 453 (S.D.N.Y. 2010). The case settled before summary judgment.

207. *See supra* Part III.D.

208. Geoffrey P. Miller, *A Modest Proposal for Fixing Delaware's Broken Duty of Care*, 2010 COLUM. BUS. L. REV. 319, 335 (2010).

209. *In re* S. Peru Copper Corp. S'holder Derivative Litig., 30 A.3d 60 (Del. Ch. 2011) (judgment on the merits), *opinion revised and superseded*, C.A. No. 961–CS, 2011 WL 6440761 (Del. Ch. Dec. 20, 2011), *enforced*, C.A. No. 961–CS, 2011 WL 6382006 (Del.Ch.

Second, the Delaware courts could revisit their decision to discard the first-to-file custom and consider speedy filing as a positive factor in contests between plaintiffs' attorneys to be named lead counsel. The Delaware courts could still disregard a fast but sloppy complaint and reward a careful, later-filed complaint, or one filed by a firm with a client with large dollars at stake, with a co-lead counsel role. Even this sort of partial reversal would give firms with good lawyers, albeit lacking a large institutional client or a track record in Delaware courts, a fighting chance.

Third, the Delaware courts could revisit their reluctance to provide expedited discovery. Doing so would move Delaware toward the median of other states and thus cancel out one of the main advantages to filing elsewhere. A grant of expedited discovery would remain discretionary, and the Delaware courts could limit the scope of discovery on a case-by-case basis to reduce the burden on defendants.

Fourth, a change in rhetoric could help. Plaintiffs' lawyers do not like to be told that the Delaware courts have "deep concerns about the agency costs imposed by plaintiffs' attorneys" (Strine in *Cox Communications*) or that most takeover cases are "worthless" (Laster in *Nighthawk Radiology*).[210] Conversely, judicial statements emphasizing the value of shareholder suits as a check on wayward or self-dealing managers could, at the margin, attract more cases.

Finally, Delaware courts could adjust the aspects of Delaware law that could lead plaintiffs' counsel to file strong cases elsewhere. For example, they could revisit the current "demand" doctrine in derivative suits, under which a plaintiff who makes demand on the board to sue the corporation's directors or officers concedes the independence of the board.[211] Predictably, almost no plaintiff ever makes demand. Some plaintiffs may currently file outside Delaware hoping for a friendlier court ruling on whether demand should be excused, even though the verbal standard for excusing demand is nominally the same. Delaware could preclude these suits from being filed elsewhere by adopting the Model Business Corporation Act approach, under which plaintiffs must make demand on the board, but are not disadvantaged by having done so.[212]

2. Discouraging Other Courts from Hearing Cases Involving Delaware Companies

When suits involving Delaware companies are filed in more than one location, the Delaware courts have a second strategy they can adopt to increase Delaware's control of corporate cases—they can encourage courts elsewhere to defer to Delaware. Delaware courts indeed are already quite willing to protect their "turf" against other courts. Delaware courts, for instance, are unlikely to grant a defendant's *forum non conveniens* motion in Delaware in favor of another state court in a corporate suit involving a Delaware company. The standard deployed is

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Dec. 20, 2011) (fee award; fee award has been appealed to Delaware Supreme Court). On the fee, see Gina Chon & Joe Palazzolo, *An Early Christmas for These Lawyers—$300 Million in Fees for Shareholder Case Sets Off Debate*, WALL ST. J., Dec. 28, 2011, at C1.

210. See *supra* notes 92 and 98 and accompanying text.

211. Spiegel v. Buntrock, 571 A.2d 767, 775 (Del. 1990).

212. MODEL BUS. CORP. ACT § 7.42 (2008).

"overwhelming hardship,"[213] which is difficult to show because under Delaware's "long arm" statute, directors and officers of Delaware companies consent to personal jurisdiction,[214] and because Wilmington, where the Chancery Court is located, is only about thirty minutes from a major airport in Philadelphia.

Delaware courts have also proved reluctant to grant a stay or a *forum non conveniens* motion in favor of another court when a suit was filed first in the other court.[215] Three cases discussed above, *In re IBP, Inc., Shareholders Litigation*, *Biondi v. Scrushy*, and *Rosen v. Wind River Systems*, illustrate the point. In each, the Chancery Court declined to stay or dismiss suits arising under Delaware corporate law, noting the presence of novel issues of Delaware law or the better framing of the Delaware complaint.[216]

Additional cases illustrate the Delaware courts' reluctance to cede jurisdiction. In *Scully v. Nighthawk Radiology*, cases arising from a takeover had been filed in Delaware and Arizona, there had been a hearing in Delaware, and a settlement of the Arizona suit was thereafter proposed.[217] When the Arizona settlement was drawn to Vice Chancellor Laster's attention, he expressed strong concern with it, because the only relief was additional disclosure by the companies involved. He ordered that the Delaware case files be sent to the Arizona court so that the Arizona judge could consider them in deciding whether to approve the settlement.

In another takeover case, *Parcell v. Southwall Technologies*, complaints were filed in Delaware and California state court.[218] On a motion by one of the defendants, Vice Chancellor Laster declined to stay the Delaware case but also declined to order expedite proceedings in Delaware. He maintained in so doing "that the one forum on these types of recurrent facts should be Delaware,"[219] commenting that the Delaware courts "necessarily have a moderate comparative advantage in adjudicating [Delaware] law."[220]

VantagePoint Venture Partners 1996 v. Examen, Inc. provides an additional illustration of Delaware judges' willingness to protect their turf. [221] The Delaware Supreme Court held that Delaware law governed a dispute over a shareholder vote in a Delaware-incorporated, California-based firm, despite a California statutory provision specifically on point, and stressed the duty of other courts, under the Full Faith and Credit Clause of the U.S. Constitution, to respect the corporate law of the state of incorporation. The decision has been interpreted as a signal to the Chancery

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213. Berger v. Intelident Solutions, Inc., 906 A.2d 134, 135 (Del. 2006); Stevelman (2009), *supra* note 10, 104–07.

214. DEL. CODE ANN. tit. 10, §§ 3114(a)–(b) (Supp. 2010).

215. Stevelman (2009), *supra* note 10, at 108–18 (reviewing the case law).

216. *See supra* notes 146–48 and accompanying text.

217. Courtroom Status Conference, Scully v. Nighthawk Radiology Holdings, C.A. No. 5890–VCL (Del. Ch. Dec. 17, 2010). This case is discussed *supra* notes 98–107 and accompanying text.

218. Teleconference, Parcell v. Southwall Techs., Inc., C.A. No. 7003–VCL (Del. Ch. Nov. 7, 2011).

219. *Id.* at *15.

220. *Id.* at *11–*12.

221. VantagePoint Venture Partners 1996 v. Examen, Inc., 871 A.2d 1108 (Del. 2005).

Court to preserve the Delaware courts' role in cases involving inter-jurisdictional conflicts.[222]

The Delaware courts do not have to be confrontational as they interact with other courts. They can also seek cooperation from judges elsewhere, signaling in so doing that they are willing to defer when a case filed in Delaware turns on federal law or the law of another state. Chancellor Chandler, in a 2011 ruling involving Allion Healthcare, Inc., suggested, for instance, that defense counsel could file motions "asking the judges in each jurisdiction to confer with one another and agree upon where the case should go forward."[223] His observations have encouraged counsel to bring such "one forum" motions in subsequent cases.[224]

Chancellor Chandler's proposal requires defense counsel to take the initiative. Moreover, even if they do so, non-Delaware judges may still be reluctant to defer to Delaware courts with a case of local import.[225] Mark Lebovitch, Jerry Silk, and Jeremy Friedman, lawyers with the Bernstein, Litowitz plaintiffs' firm, have proposed in the M&A context a more elaborate scheme designed to channel litigation to Delaware courts.[226] They propose that the Delaware Chancery Court require the first plaintiff to file a complaint against a merger in the Chancery Court to publish national notice of the action. The notice would trigger a 10 day period during which any other plaintiffs' firm interested in challenging the transaction could submit a case management plan that explained why its shareholder-lawyer pair should be named lead plaintiff and lead counsel. The Chancery Court would then apply the *TCW Technology* factors to choose the lead plaintiff and lead counsel for the Delaware suit. Lebovitch, Silk, and Friedman predict that judges elsewhere would often defer to Delaware courts with this framework in place because the judges would surmise that a firm filing in their court had chosen not to participate in an "open and transparent leadership process," and could expect Delaware's courts to cede jurisdiction in appropriate cases by staying the Delaware action.[227]

C. Will the Delaware Courts Seek to Regain Market Share?

While there are a number of steps the Delaware courts could take to regain case flow market share, for various reasons we spell out now, it cannot be taken for granted that Delaware courts will take any of these steps.

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222. Stevelman (2009), *supra* note 10, at 88; Glynn (2008), *supra* note 196, at 137.

223. *In re* Allion Healthcare Inc. S'holders Litig, C.A. No. 5022–CC, 2011 WL 1135016, at *4 n.12 (Del. Ch. Mar. 29, 2011).

224. *See supra* note 38 and accompanying text; Micheletti & Parker (2012), *supra* note 10, at 34–35.

225. David Marcus, *The Chancellor's Proposal*, DEAL MAG., Apr. 25, 2011, http://www.thedeal.com/magazine/ID/039137/2011/the-chancellors-proposal.php.

226. Lebovitch, Silk & Friedman (2011), *supra* note 78.

227. *Id.* at 8.

1. The Reaction of Delaware Companies

If the Delaware courts seek to regain litigation market share, a major concern would be the reaction of Delaware companies. How, to return to the title of this Article, can Delaware balance a manager-friendly approach, which will attract and retain incorporations, with a stance sufficiently friendly to plaintiffs' lawyers to attract shareholder lawsuits?

Historically, Delaware succeeded in attracting both managers and plaintiffs' lawyers. Correspondingly, it might be thought that the Delaware courts could readily backtrack from steps that have jeopardized their popularity among plaintiffs' attorneys without losing incorporation market share. Nevertheless, adoption of an explicitly litigation-friendly posture by Delaware judges could make corporate managers uneasy. As Douglas Branson has observed, "Overly generous fee awards and excessive litigation . . . unduly burden corporate treasuries and are inimical to longer term shareholder interests."[228]

At the same time, many Delaware companies might not respond too adversely to some steps that the Delaware courts could take. Suppose, for example, that Delaware became more "fee-friendly" in cases where plaintiffs' lawyers achieve a significant recovery while remaining niggardly on fees for "disclosure-only" settlements in cases arising from arm's length takeovers. The message to plaintiffs' lawyers might be, "to obtain a real fee, obtain a real recovery." The *Southern Peru*, case discussed above, in which the court awarded a $300 million fee for a $2 billion recovery, fits this pattern.

How might shareholders and corporate directors react if Delaware courts do become more generous in awarding fees in cases with large dollar recoveries? Institutional shareholders might like such an arrangement. Many directors would prefer no suits and no fees, but might not object too strongly. The Delaware courts, by rewarding only real recoveries, would be discouraging "file on every deal" lawsuits, even if this only meant that the suits were filed elsewhere.

Delaware companies might also not object much to changes to the approach used for selection of lead counsel. If Delaware judges gave greater weight to early filing when resolving lead counsel disputes, defendants might welcome a modestly resourced rapid filer as lead opposing counsel. Delaware firms might also not object to easier plaintiff access to expedited discovery in Delaware, given the likely alternative of expedited discovery elsewhere, supervised by a less knowledgeable judge. And a change in rhetorical tone, unless accompanied by a significant change in substantive outcomes, should not materially disadvantage Delaware companies or their directors. Correspondingly, so long as the Delaware courts do not reverse field too dramatically, they likely could move in a litigation-friendly direction without jeopardizing Delaware's popularity for incorporations.

2. Reputational Concerns

If the Delaware courts take steps to bring back case flow, they will need to be sensitive about how they do so. Aggressive efforts to recapture market share could

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228. Branson (1990), *supra* note 27, at 102.

jeopardize their reputation as elite, national arbiters of corporate law. Past efforts by the Delaware courts to assert control over cases with multi-jurisdictional filings illustrate the point. Commentators have described attempts by Delaware courts to obtain or retain jurisdiction in corporate law cases as "transparently self-interested"[229] and termed the constitutional law analysis in *VantagePoint* "gratuitous" and an example of "remarkable overbreadth."[230] Likewise, after Vice Chancellor Laster indicated in *Scully v. Nighthawk Radiology Holdings Inc.* that the lead defense litigator, David Berger, might lose his *pro hac vice* right to appear in Delaware, various litigators described the judge's treatment of Berger as unfair.[231]

If Delaware implemented Lebovitch, Silk, and Friedman's proposal that plaintiffs' attorneys file M&A claims in Delaware courts within a specified time, the reaction might be similar. Plaintiffs' lawyers who knew they were unlikely to gain lead counsel status in Delaware and thus did not file there, might complain to their preferred court about the Delaware courts' exclusionary tactics as part of an effort to persuade that court to retain jurisdiction. More generally, as the special counsel appointed in *Scully* noted in his 2011 report, "There is also the danger that an attempt by a single court to solve these multi-jurisdictional issues will be resisted by other courts or avoided by litigants."[232]

3. Resource Constraints

The discussion above assumes that the Delaware judges want to recapture market share and asks whether and how they can do so. But perhaps they will not want many of the cases they are losing. The Delaware judges' turn against the first-to-file presumption, their fee cuts, and their rhetorical tone reflect a sense that many current suits should not be brought. This may be a reasonable reaction. A securities litigator has described the business model of some plaintiffs' firms as "a numbers game. The contingency fees [for M&A suits] are actually pretty small . . . , so the business model is based on the volume of payouts."[233] For Delaware judges recapturing control of high-volume, low-expected payout suits may be an unappetizing prospect. For these cases, managing the case load is often largely an administrative function, involving little more than addressing motions to expedite discovery and approving proposed settlements. These cases may also do little to develop Delaware's case law.

Concerns about scarce judicial resources could reinforce reluctance among Delaware judges to recapture litigation market share. There are only five Delaware Court of Chancery judges, and they have limited capacity to deal with new cases, even if much of the work is administrative. To be sure, the number of Chancery court judges could be increased, but that could be unattractive to the sitting judges because it would dilute their influence and might decrease the overall coherence of

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229. Glynn (2008), *supra* note 196, at 118.

230. Stevelman (2009), *supra* note 10, at 88.

231. David Marcus, *Multiforum Mayhem*, DEAL MAG., Jan. 21, 2011, http://www.thedeal.com/magazine/ID/038069/2011/multiforum-mayhem.php.

232. Brief of Special Counsel Gregory P. Williams, at 32, Scully v. Nighthawk Radiology Holdings, Inc., C.A. No. 5890–VCL (Del. Ch. Mar. 11, 2011).

233. MacFadyen (2010), *supra* note 51.

Delaware law. Indeed, if tough regulation of attorneys' fees and a distaste for hasty filers primarily discouraged weak claims, the Delaware judges might happily sacrifice litigation market share and devote the judicial resources available to the complicated cases where their expertise would be most valuable.

A key question, then, is whether Delaware is losing good cases as well as bad. The likely answer is at least sometimes "yes," as illustrated by our options backdating cases. Our lawyer-interviewees viewed many of these cases as strong, yet the vast majority were filed outside Delaware.[234] The judgment about claim strength was confirmed by some sizeable settlements. Among our 165 companies facing options backdating derivative suits, 52 resulted in a cash settlement, with aggregate payments of nearly $2.1 billion.[235] Settlements of $900 million involving UnitedHealth Group (incorporated in Minnesota) and $600 million involving Cardinal Health (incorporated in Ohio) accounted for more than half of this total.[236] There were, however, 14 other options backdating cases with settlements of $10 million or more, 10 involving Delaware companies. In only one of these 10 cases, involving NVIDIA Corp., was a suit brought in Delaware. A suit against NVIDIA was also brought in California; the two suits were settled together.

The fact that a number of the most cited Delaware corporate cases, such as *Aronson v. Lewis*,[237] *Weinberger v. UOP*,[238] and *Kahn v. Lynch Communications*,[239] were brought by individuals who were "professional" plaintiffs owning only a few shares also implies Delaware's current approach could be costing Delaware good cases as well as bad. Could the lawyers who brought these cases have found institutional clients and secured a lead counsel role under Delaware's current approach? There is no way to know, but the answer might often be no, meaning that these potentially important cases might today be filed and heard outside Delaware.[240]

Even major plaintiffs' firms that have the professional reputations and institutional clients likely to yield lead counsel appointments in Delaware may bring some of their "good" cases elsewhere. In our interviews with plaintiffs' lawyers a number stressed that they treat filing in Delaware as a serious option but may well choose to file elsewhere, with the choice turning on a number of factors.

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234. *See supra* Part II.B.4.

235. This is a lower bound on the number of settlements with payments. Our principal source for many of the settlements was the company's disclosure in its 10-K annual report. Companies need only disclose "material pending legal proceedings," 17 CFR § 229.103 (2011); SEC Regulation S-K Item 103. A fair number of companies in our dataset disclosed the lawsuit but did not disclose the outcome.

236. For details on these settlements, see Kevin M. LaCroix, *UnitedHealth Derivative Settlement "Largest Ever,"* D&O DIARY (Dec. 6, 2007), http://www.dandodiary.com/2007/12/articles/options-backdating/unitedhealth-derivative-settlement-largest-ever/ (UnitedHealth); Kevin M. LaCroix, *More Options Backdating Lawsuit Dismissals and Settlements*, D&O DIARY (May 16, 2007), http://www.dandodiary.com/2007/05/articles/options-backdating/more-options-backdating-lawsuit-dismissals-and-settlements/ (Cardinal Health).

237. Aronson v. Lewis, 473 A.2d 805 (Del. 1984)

238. Weinberger v. UOP, Inc., 457 A.2d 701 (Del. 1983)

239. Kahn v. Lynch Commc'n Sys., 638 A.2d 1110 (Del. 1994).

240. *See* Quinn (2011), *supra* note 10, at 24.

When they file elsewhere, sometimes the cases will be strong ones. Indeed, the plaintiffs' lawyers we interviewed emphasized that it is often hard to know how strong a case they have at the time of filing. Accordingly, when major plaintiffs' firms sue outside Delaware, Delaware likely loses at least some good cases.

Various features of Delaware litigation likely encourage major plaintiffs' firms to file outside Delaware. The fact that Delaware courts have chopped fees in some cases with large recoveries[241] will be one factor, perhaps a large one if the lawyers think they might receive more elsewhere. Some of our interviewees cited the anti-plaintiffs'-lawyer rhetoric of some Delaware cases as a reason to avoid Delaware, even if it has not (yet) been directed at them.

Also, when plaintiffs' lawyers suffer adverse outcomes in Delaware, they may attribute the setbacks to anti-plaintiff bias, rightly or wrongly. Vice Chancellor Laster's remarks in a 2011 takeover case concerning plaintiffs' lawyer Richard Brualdi illustrate how encounters with Delaware judges can dissuade plaintiffs' lawyers from suing in Delaware. Vice Chancellor Laster observed that Brualdi had not been eager to come back to Delaware after Vice Chancellor Lamb had declined to approve a settlement in a case where Brualdi was lead counsel on the basis that he had failed to represent the interests of the class adequately.[242] Or as one lawyer, who has obtained large recoveries in Delaware, said to us in 2011 about a hearing outcome: "After yesterday's joke of a [Delaware] hearing in my [name deleted] case, you better believe [I'll be interested in] suing outside of Delaware so [my clients] get a fair shake!"[243]

The upshot is that the out-of-Delaware trend is likely causing Delaware courts to lose both "good" and "bad" cases. Conversely, an effort to recapture market share will likely mean that the Delaware courts would face a higher volume of both types of cases, a potentially unappealing prospect due to resource constraints.

4. Efforts to Recapture Market Share May Fail

Assume now that Delaware judges, having taken into account possible reputational damage and resource constraints, are convinced a loss of "market share" with respect to cases filed is seriously detrimental to Delaware's interests and are inclined to seek to correct matters. A final obstacle to proceeding would be that their efforts might not succeed, or might have only a modest effect, especially in the near term. Plaintiffs' attorneys, having had their or their brethren's motives impugned with some regularity, might not quickly forgive and again take their chances by filing in Delaware. Similarly, given Delaware's record in cutting fee requests in both good cases and bad, it may take a period in which awards for cases with real recoveries are comparable to what plaintiffs' counsel could expect elsewhere before counsel will trust their fate on this issue, so crucial for them, to the Delaware courts. With regard to expedited discovery, a change in the Delaware

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241. *See supra* Part III.D.

242. Teleconference at *13–*14, Parcell v. Southwall Techs., Inc., C.A. No. 7003–VCL (Del. Ch. Nov. 7, 2011).

243. This lawyer is among those who advised us that his firm decides on a case by case basis whether to file in Delaware or elsewhere.

court rules might well be needed to convince plaintiffs' lawyers that this will be as readily available to them in Delaware as elsewhere.

V. OTHER POTENTIAL RESPONSES TO THE OUT-OF-DELAWARE TREND

While it is unclear which steps, if any, the Delaware judiciary will take to reverse or limit the migration of corporate cases out of Delaware, or how well any judicial efforts would succeed, Delaware companies, the Delaware legislature or Congress perhaps could take steps that could reverse or limit the out-of-Delaware trend.

A. Self-Help by Delaware Companies

Delaware companies and their lawyers have various strategies they can adopt to influence venue. One possibility is to respond *ex post* by bringing a stay, dismissal, or one forum motion to try to channel litigation to a preferred jurisdiction.[244] Another, and the one focused on here, is for companies to act *ex ante* and adopt charter or bylaw provisions specifying Delaware as the exclusive forum for shareholder claims against directors.

Delaware is a popular forum among many lawyers who advise public companies. For example, Stephen Radin, a senior litigation partner at Weil, Gotshal & Manges, said of the Delaware Court of Chancery in a 2004 interview: "It is a great court. There is a Chancellor and four Vice Chancellors. Each is expert in corporate law. I wish more of my practice was in Delaware."[245] Similarly, Kenton King of Skadden Arps said in 2006 with regard to other courts applying Delaware law heard outside Delaware: "What I tell clients is that even though Delaware law is being applied, when it's being applied by a bench that doesn't have as much familiarity with these cases, the predictability goes down . . . ."[246] Lawyers who believe that litigating in Delaware serves their corporate clients' interests could urge those clients to adopt charter or bylaw provisions selecting Delaware as the exclusive forum for litigation. When Wachtell Lipton partner Ted Mirvis drew attention to the out-of-Delaware trend in 2007 that was his proposed cure.[247] Vice Chancellor Laster endorsed forum selection clauses in *Revlon* in 2010.[248] At least one law firm thereafter told clients in the wake of the *Revlon* decision that a forum selection clause was the new "must" for Delaware companies.[249]

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244. *See supra* notes 35–38 and accompanying text.

245. *A Corporate Governance Practitioner on the Delaware Courts*, METROPOLITAN CORP. COUNS., Nov. 2004, at 47.

246. Marcus (2006), *supra* note 66.

247. *Anywhere but Chancery* (2007), *supra* note 1.

248. *In re* Revlon Inc. S'holders Litig., 990 A.2d 940, 960 (2010) ("If boards of directors and stockholders believe that a particular forum would provide an efficient and value-promoting locus for dispute resolution, then corporations are free to respond with charter provisions selecting an exclusive forum for intra-entity disputes.").

249. Latham & Watkins, *Designating Delaware's Court of Chancery as the Exclusive Jurisdiction for Intra-Corporate Disputes: A New 'Must' for Delaware Company Charter or Bylaws*, CORP. GOVERNANCE COMMENT., Apr. 2010, *available at*

Delaware-only forum selection clauses are becoming more common.[250] One study found that the number of Delaware firms that had adopted or proposed such provisions grew from 82 as of April 2011 to 195 by year-end.[251] The *Revlon* decision appears to have generated momentum in favor of forum selection clauses, as only 16 forum selection provisions had been adopted before it.[252] The growth in multi-forum litigation could, over time, prompt even more companies to seek to adopt forum selection clauses.

Even if managers of Delaware companies—or, in practice, their lawyers—become persuaded that a Delaware-only forum selection clause is a good idea, this might not greatly affect the out-of-Delaware trend. Stockholder resistance is one potential obstacle. Even institutional shareholders who respect the expertise of the Delaware judiciary could balk at giving up their current freedom to choose to sue elsewhere. Institutional investors that partner with some regularity with plaintiffs' law firms—particularly public pension funds[253]—could be especially wary about being tied down in this way.

The enforceability of a Delaware forum selection provision is also uncertain. Traditionally, state and federal courts refused to enforce forum selection clauses in contract disputes, reasoning that these terms were void as against public policy because courts were being ousted of their jurisdiction.[254] However, in 1972 the United States Supreme Court held in *M/S Bremen v. Zapata Off-Shore Co.* that forum selection clauses are *prima facie* valid and should be upheld unless the resisting party could show enforcement would be unreasonable under the circumstances.[255] A judge asked to determine the enforceability of a Delaware forum selection provision could accept, as Delaware courts do, that a corporation's charter and bylaws are analogous to a contract,[256] and honor the provision. But this is far from certain.

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http://www.lw.com/upload/pubContent/_pdf/pub3510_1.pdf.

250. *See* Lewis (2008), *supra* note 10, at 202–03.

251. Claudia H. Allen, *Study of Delaware Forum Selection in Charters and Bylaws*, NEAL, GERBER & EISENBERG LLP, Jan. 25, 2012, *available at* http://www.ngelaw.com/pubs/uniEntity.aspx?xpST=PubDetail&pub=623 (provides URL link to request complete study).

252. Grundfest (2010), *supra* note 7, at 3, 7.

253. Some law firms even make campaign contributions to public pension officials seeking re-election. See, for example, Mark Maremont, Tom McGinty & Nathan Koppel, *Trial Lawyers Contribute, Shareholder Suits Follow*, WALL ST. J., Feb. 3, 2010, http://online.wsj.com/article/SB10001424052748703837004575013633550087098.html.

254. Walter W. Heiser, *Forum Selection Clauses in State Courts: Limitations on Enforcement After* Stewart *and* Carnival Cruise, 45 FLA. L. REV. 361, 366–67 (1993).

255. M/S Bremen v. Zapata Off-Shore Co., 407 U.S. 1 (1972). This holding was limited to admiralty jurisdiction and international commercial contracts, but lower federal courts and state courts in many jurisdictions have applied the reasoning in other contexts. *See* Heiser (1993), *supra* note 254, at 363, 367–72.

256. Centaur Partners, IV v. Nat'l Intergroup, Inc., 582 A.2d 923, 928 (Del. 1990) ("Corporate charters and by-laws are contracts among the shareholders of a corporation and the general rules of contract interpretation are held to apply."); Jackson Walker LLP v. Spira Footware, Inc., C.A. No. 3150–VCP, 2008 WL 2487256, at *4 (Del. Ch. June 23, 2008) ("A company's bylaws are contractual in nature.").

Some forum selection provisions do not require cases to be brought in Delaware courts but instead give a board the choice to remove a case to Delaware or not.[257] Courts outside Delaware might balk at giving the defendants in a lawsuit that degree of discretion. Moreover, some forum-selection clauses are bylaws, adopted unilaterally by boards of directors.[258] This weakens the analogy to contracts, and the lack of shareholder consent might give pause to some courts. Courts would be more likely to respect a Delaware-only charter provision because amendments to a corporate charter must be approved by the shareholders.[259]

The limited case law indicates that the enforceability of forum selection provisions cannot be taken for granted. In *Galaviz v. Berg*, the Northern District of California declined to enforce a Delaware-only bylaw adopted by the Oracle Corporation board.[260] The court declined to treat the bylaw in question as being akin to a contractual term, reasoning that the directors had acted unilaterally without shareholder consent, but did suggest that there would be a stronger case for honoring a venue provision in a corporate charter.[261]

One might also question whether a Delaware-only venue provision, even if in a corporate charter, would be enforced if a case is brought in federal court that includes both state claims and federal claims, most likely under federal securities law. In those instances the Delaware courts will usually lack subject matter jurisdiction over the federal claims.[262] Would the federal court be willing to dismiss the corporate law claims, thus forcing the plaintiffs to proceed in two jurisdictions instead of one? The answer is unknown. The enforceability in federal court of agreements compelling litigation to proceed in state court, especially if the claims could be combined with an ongoing federal suit, is a complex issue that has received little academic attention.[263]

B. Delaware Legislation

The Delaware legislature conceivably could intervene directly to encourage corporate suits to proceed in Delaware. There have been previous instances where the Delaware legislature has facilitated litigation before the Delaware courts. For example, Delaware has given other state and federal courts, as well as the Securities and Exchange Commission, the right to certify questions of Delaware law to the Delaware Supreme Court, which will resolve them.[264] Likewise, in 2003

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257. Grundfest (2010), *supra* note 7, at 6 (indicating that 8 of 25 forum selection provisions studied were "elective" and gave the board *ex post* discretion on whether to compel litigation to occur in the state of incorporation or allow it to proceed in another state. The others were mandatory, so litigation had to proceed in the state of incorporation.).

258. *Id.* at 6, 19 (Nine of the 25 forum selection provisions studied were by-laws.).

259. DEL. CODE ANN. tit. 8, § 242(b)(1) (2010).

260. Galaviz v. Berg, 763 F. Supp. 2d 1170 (N.D. Cal. 2011).

261. *Id.* at 1174–75.

262. 15 U.S.C. § 78aa (2006) (giving the federal courts exclusive jurisdiction over these claims).

263. *See* Michael D. Moberly, *Judicial Protection of Forum Selection: Enforcing Private Agreements to Litigate in State Court*, 1 PHOENIX L. REV. 1, 4, 55 (2008).

264. DEL. SUP. CT. R. 41; Henry duPont Ridgely, *Avoiding the Thickets of Guesswork:*

Delaware's expanded its "long arm" statute, under which directors of Delaware firms are deemed to consent to personal jurisdiction in Delaware, to officers as well.[265]

Going forward the Delaware legislature could, as Brian Quinn has suggested, amend Delaware corporate law to authorize companies to include Delaware-only forum selection clauses in their charters for suits against officers or directors.[266] This would not guarantee that another court would honor such a charter amendment, but might make this outcome more likely. The legislature could additionally encourage Chancery Court judges to promote litigation in Delaware courts by increasing the number of vice-chancellors, thus reducing the burden on each. It could also expand plaintiff rights to expedited discovery, at least in time-sensitive takeover cases. The possibilities are many. Even more so than for responses by the courts, one can only speculate on what the legislature might do, and how effective any action would be.

C. Federal Reform

The out-of-Delaware trend could also elicit a federal response. For instance, the New York City Bar Association's Committee on Securities Litigation has proposed federal reforms that would limit multi-jurisdictional corporate litigation by channeling suits to the state of incorporation—hence often to Delaware.[267] But one can also imagine federal reform that would largely sideline the Delaware courts, at least in shareholder class action suits. Recall that SLUSA contains a so-called "Delaware carve-out" from general provisions that preempt state securities class actions.[268] The Class Action Fairness Act of 2005, which permits defendants to remove state class actions to federal court, contains a similar exception for class actions under corporate law.[269] Delaware courts dealing with corporate litigation were assumed, contrary to the general trend with state courts, to offer a safe pair of hands that rendered unnecessary a diversion of these suits to the federal courts.[270]

With many corporate class actions now being filed in state courts other than Delaware, the justification for the carve-out is weakened. One plausible federal response would be to limit the carve-out to shareholder class actions brought in the state of incorporation. Such a change would mean lawsuits of this type involving Delaware companies would have to be brought in Delaware courts, which would help to reverse the out-of-Delaware trend. Another possibility would be to eliminate the carve-out entirely. This would channel shareholder class actions to

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The Delaware Supreme Court and Certified Questions of Corporate Law, 63 SMU L. REV. 1127, 1131–32 (2010); *see also* DEL. CONST. art. IV, 11(8). The certification power was created in 1984 and extended to the SEC in 2007. duPont Ridgley (2010), *supra*, at 1131.

265. DEL. CODE ANN. tit. 10, § 3114(b) (Supp. 2010).

266. Quinn (2011), *supra* note 10, at 38–43; *see also* Stevelman (2009), *supra* note 10, at 135; Micheletti & Parker (2012), *supra* note 10, at 36–37.

267. COMMITTEE ON SECURITIES LITIGATION (2008), *supra* note 68, at 9.

268. *See supra* note 173 and accompanying text.

269. Class Action Fairness Act of 2005, Pub. L. No. 109-2, § 5, 119 Stat. 4, 13 (codified at 28 U.S.C. § 1453(d)(2)–(3) (2006)).

270. *See* Johnson (2012), *supra* note 10, at 53; Strine (2001), *supra* note 14, at 1257, 1273.

federal courts and be a blow to Delaware. The desirability of such changes would depend to a considerable degree on whether the out-of-Delaware trend is beneficial, the topic to which we turn next.

VI. THE PROS AND CONS OF THE OUT-OF-DELAWARE TREND

We have thus far assessed the likely reasons for the out-of-Delaware trend, and how various actors might respond. We turn in this Part to a brief and tentative assessment of whether the trend is likely to be good or bad for shareholders, who in large measure bear whatever costs and earn whatever benefits come with the uniquely American practice of frequent shareholder litigation.[271] We assume initially that there will not be a major erosion of Delaware's incorporation market share and focus on forum shopping.

A. The Mixed Implications of Forum Shopping

Forum shopping sounds unsavory, and is often denounced on the grounds that it allows litigants to manipulate lawsuit outcomes.[272] There is also an obvious inefficiency if suits are filed in more than one jurisdiction.[273] As Chancellor Strine said about multi-jurisdictional M&A litigation at a 2011 conference on Delaware courts and corporate law, "These are suits about a single transaction where one authoritative and timely ruling is required. Competing proceedings are not only inefficient, but bad for investors and our economy."[274] Yet forum shopping can also be thought of more charitably from a market perspective. Litigants, under this analogy, constitute the demand side, judges constitute the supply side, and the competitive discipline imposed by litigant choice can improve the quality and speed of judicial decision-making.[275]

To take a concrete example, it is plausible that expedited discovery in M&A suits, followed by a preliminary injunction hearing well before the shareholder meeting to vote on the merger, imposes useful discipline on the merging parties, even if most suits generate no financial recoveries. Currently, however, expedited discovery is not reliably available in Delaware.[276] Out-of-state filings put pressure on Delaware to grant expedited discovery more liberally. Thus, forum shopping

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271. *See generally* John Armour, Bernard Black, Brian Cheffins & Richard Nolan, *Private Enforcement of Corporate Law: An Empirical Comparison of the United Kingdom and United States*, 6 J. EMPIRICAL LEGAL STUD. 687 (2009) (contrasting the litigation-rates in the United States and Britain).

272. *See, e.g.*, Bassett (2006), *supra* note 35, at 388; *Forum Shopping Reconsidered*, *supra* note 35, at 1680.

273. Johnson (2012), *supra* note 10, at 44–47 (making this point for takeover suits); Quinn (2011), *supra* note 10, at 5, 9; COMMITTEE ON SECURITIES LITIGATION (2008), *supra* note 68, at 9.

274. *The Dramatic Increase in M&A Litigation*, DAILY DEAL, Nov. 28, 2011, http://www.thedeal.com/magazine/ID/043019/commentary/the-dramatic-increase-in-m&a-litigation.php.

275. Zywicki (2006), *supra* note 108, at 1146–47.

276. *See supra* note 178 and accompanying text.

may generate more benefits than costs in this instance. To assess the benefits and costs of forum shopping for other types of corporate lawsuits, one must study the institutional context in which each arises. This is no easy task, and would likely fail to yield definitive conclusions.[277]

B. Quality of Judicial Decision-Making

Given the respect widely accorded to the Delaware Chancery Court, one might think that if many cases are filed elsewhere, the average quality of judicial decision-making in corporate cases will decline. The Delaware judiciary's familiarity with business dynamics, reinforced by a steady flow of corporate cases, may well be lacking elsewhere.[278] The United States could also lose the de facto national corporate law it presently benefits from. As Chancellor Strine said in *In re Topps Co. Shareholders Litigation*, the "important coherence-generating benefits" of Delaware courts will be at risk if "decisions are instead routinely made by a variety of state and federal judges who only deal episodically with our law."[279] Yet there could be countervailing gains from sizeable numbers of corporate cases involving Delaware companies being filed elsewhere.

One consideration is that judges elsewhere may in some instances develop expertise akin to that present in Delaware. For example, many corporate suits are brought in the Complex Case Division of the Santa Clara County Superior Court. This small (three judges) court has correspondingly developed considerable familiarity with corporate cases, many of which involve Delaware law.[280] So too for judges on specialized business courts in some other states, and for federal district court judges—notably in the Northern District of California and the Southern District of New York—who regularly hear corporate and securities cases.

Just as Delaware Court of Chancery judges take pride in their expertise, and surely like to be involved in important cases, so, at least potentially, do judges elsewhere. Some of those judges may compete to receive major cases. The Delaware judges will also need to compete to keep case flow. Is that competition for good or ill? There is no clear answer, but there may well be circumstances where rulings from outside Delaware could impose a salutary discipline on the development of Delaware case law. This could be the case with director liability, for example.

A case can be made that independent directors acting honestly should face *some* risk of personal liability for severe dereliction of duty, even without self-dealing.[281]

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277. Zywicki (2006), *supra* note 108, at 1148, 1157–60 (concluding after examining Delaware corporate law that it is unclear whether forum shopping is a good or bad thing).

278. Klausner (1995), *supra* note 16, at 845–46 ("[O]nce a judge is appointed, his or her performance in the corporate law area . . . will depend at least in part on the number of corporate law cases the court hears.").

279. *In re* Topps Co. S'holders Litig., 924 A.2d 951, 959 (Del. Ch. 2007).

280. Wilson Sonsini Goodrich & Rosati, *Restricting Shareholder Derivative Suits to Delaware: Stop, Look and Listen* (Jan. 2011), http://www.wsgr.com/publications/PDFSearch/wsgralert_delaware_shareholder_derivative_suits.pdf.

281. For the views of two of us, see Bernard Black, Brian Cheffins & Michael Klausner, *Outside Director Liability*, 58 STAN. L. REV. 1055 (2006); Bernard Black, Brian Cheffins &

As we have seen, however, Delaware courts have adopted a tough "conscious disregard of duty" standard for a plaintiff to show director lack of good faith at companies which have adopted Section 102(b)(7) charter provisions to eliminate director liability absent self-dealing or lack of good faith. The Delaware courts have never found the "conscious disregard" standard to have been met. Currently, the leading cases finding evidence sufficient (or, on a motion to dismiss, potentially sufficient) to meet the standard come instead from outside Delaware.[282] Could the judgments of other courts on what meets this standard prompt a beneficial change of approach by Delaware courts? If independent directors face a somewhat greater risk of personal liability if a case involving a Delaware company is heard outside Delaware, is that good or bad? The answers to these questions are by no means clear. Still, as this example suggests, forum competition may in some circumstances have a beneficial impact on the quality of judicial decision-making, even if Delaware courts have the final say in developing precedents.

C. Impact on the Delaware Brand

We have pointed out that while a loss of litigation market share by Delaware could cause a significant loss in market share for incorporations, it is unclear whether this will occur. Still, suppose the loss of litigation market share would lead to some long-term weakening of Delaware's market share for incorporations. That would be a bad outcome for Delaware's tax base and its in-state lawyers and judges, but would it occasion a broader social loss?

Those who see "race to the bottom" elements in Delaware's dominance might cheer. For those inclined to see Delaware as having won "a race to the top," and providing more efficient law than other states, the situation is more complicated. On one hand, if Delaware's market share were to decline, so would the network benefits of Delaware incorporation.[283] On the other hand, if regulatory competition is often salutary, as many race-to-the-top proponents believe,[284] stronger forum competition might push Delaware to improve its law.

VII. CONCLUSION

For at least half a century the Delaware courts have been the de facto "national" U.S. corporate law courts. Delaware law is a central part of the business law curriculum in most major U.S. law schools.[285] The official comments accompanying the Model Business Corporations Act (MBCA), a model law followed by twenty-four states,[286] frequently refer to Delaware cases to provide

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Michael Klausner, *Outside Director Liability: A Policy Analysis*, 162 J. INSTITUTIONAL & THEORETICAL ECON. 5 (2006).

282. *See supra* notes 205–06 and accompanying text.

283. On the network benefits associated with Delaware incorporation, see Klausner (1995), *supra* note 16, 843–47.

284. *See, e.g.*, ROMANO (1993), *supra* note 15.

285. Simmons (2008), *supra* note 17, at 1173; WILLIAM T. ALLEN, REINIER KRAAKMAN & GUHAN SUBRAMANIAN, COMMENTARIES AND CASES ON THE LAW OF BUSINESS ORGANIZATION xxiii (3d ed. 2009) (explaining the authors' decision to focus on Delaware cases).

286. MODEL BUS. CORP. ACT ANNOTATED xii (4th ed. 2008).

examples to explain the drafters' choices.[287] Courts in other states often cite and follow Delaware case law when their own case law is sparse. Courts in MBCA states sometimes cite Delaware jurisprudence in preference to decisions from other MBCA states.[288]

Given the Delaware courts' dominance in writing leading corporate law decisions, and given Delaware's dominance as the incorporation locus for publicly traded companies, one might expect Delaware to be the venue of choice for suits under corporate law involving Delaware-incorporated firms. And so it once was, but less so now. In this Article, we make this point by summarizing the evidence we develop in a companion empirical article on Delaware's loss of litigation market share. We then explore the reasons for the out-of-Delaware trend, the steps the Delaware judges or legislature, or Delaware companies, might take to reverse this new trend and the implications of the trend for the quality of corporate law.

Delaware's loss of litigation market share suggests that a delicate balancing act engaged in by Delaware and its courts could be going awry. To attract incorporations, Delaware must appeal to corporate managers without being so pro-manager as to disturb shareholders. In that effort, Delaware's expert judges and well-developed case law are major selling points. Yet Delaware needs continued case flow to generate precedents on which the users of Delaware corporate law depend. Plaintiffs' attorneys, however, will only file suits in Delaware courts if they expect better results in Delaware than elsewhere. Increasingly, they do not. The principal reasons appear to include anti-plaintiff-lawyer rhetoric in some cases, fee cuts for plaintiffs' lawyers, the weakening of the custom which gave early filers an edge in the battle for the lead counsel role and greater ease in obtaining elsewhere expedited discovery.

It must be tempting for Delaware courts to take steps to recapture market share. They are aware of the out-of-Delaware trend, as they have referred in a number of recent rulings to the multi-jurisdictional "problem."[289] Moreover, some of the changes in Delaware law and practice that likely contributed to the trend could probably be reversed without engendering strong opposition from corporate managers. How the Delaware courts will respond, and how successful any response will be, remains to be seen. Delaware firms could also respond by adopting forum selection clauses. Some have done so but the enforceability of forum selection provisions, particularly bylaws, is unclear. Moreover, if major institutional shareholders either favor, or become troubled by, the out-of-Delaware trend, they likely could influence where cases are filed. But major shareholders have thus far been silent. Correspondingly, it is too soon to know whether the Delaware courts can successfully rebalance their approach to litigation in order to regain litigation market share without undermining Delaware's success in attracting incorporations.

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287. William B. Chandler III & Anthony A. Rickey, *Manufacturing Mystery: A Response to Professors Carney and Shepherd's "The Mystery of Delaware Law's Continuing Success,"* 2009 U. ILL. L. REV. 95, 113.

288. *Id.* at 114–15; Scott R. Haiber, *Derogating the Derivative:* Tandycrafts Inc. v. Initio Partners *and the Role of Attorneys' Fees in Shareholder Litigation*, 3 DEPAUL BUS. L.J. 213, 242 (1990).

289. Micheletti & Parker (2012), *supra* note 10, at 27.

The policy implications of the out-of-Delaware trend are unclear as well. The market for incorporations works imperfectly, not least because incorporation decisions are often made by self-interested managers, loosely policed by shareholders. The shareholder litigation market surely works imperfectly as well, not least because forum choices are often made by self-interested plaintiffs' lawyers, often only loosely policed by shareholders.[290] Given these twin imperfections, the social welfare effects of the out-of-Delaware trend are unclear. Nevertheless, the trend has emerged as an important feature of U.S. corporate law that will likely attract the attention of judges, lawyers, and academics for some time.

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290. Grundfest (2010), *supra* note 7, at 17.

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