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A THEORY OF REPRESENTATIVE SHAREHOLDER SUITS AND ITS APPLICATION TO MULTIJURISDICTIONAL LITIGATION

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ABSTRACT—We develop a theory to explain the uses and abuses of representative shareholder litigation based on its two most important underlying characteristics: the multiple sources of the legal rights being redressed (creating dynamic opportunities for arbitrage) and the ability of multiple shareholders to seek to represent the collective group in such litigation (creating increased risk of litigation agency costs by those representatives and their attorneys). Placed against the backdrop of controlling managerial agency costs, our theory predicts that: (1) the relative strength of the different forms of shareholder litigation will shift over time, (2) these shifts can result in new avenues for the shareholders to express litigation power, (3) new agents will emerge to act on shareholders' behalf when these shifts occur (or old agents will put on new hats), and (4) a new set of principal-agent costs resulting from litigation will arise out of these new relationships, leading to recurrent questions about how to best control these costs in particular contexts. Applying our theory to recent academic and practitioner claims of abusive multijurisdictional forum shopping in representative corporate litigation, we conclude that these claims are both overstated and misdirected. Instead, we find a significant amount of what we call “fee distribution litigation.” In these cases, multijurisdictional suits are filed by plaintiffs' law firms largely to obtain a slice of the total pool of plaintiffs' attorneys' fees that are paid in a global settlement in one of these cases. We show that fee distribution litigation is quite different than traditional forum shopping and requires a different policy response. We then consider various approaches and conclude that, while no one of them is perfect, judicial comity is the best and least costly option.

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INTRODUCTION

In an ancient Indian fable, six blind men touch an elephant to try to understand what it is. Each of them feels a different part of the animal and says what he thinks the elephant looks like based on what he has felt; since they each touch a different segment of the elephant, their descriptions are so different that they cannot possibly be describing the same thing. In one version of the story, the rajah then explains to them that they are all right because the elephant has all of the features that they have mentioned, but that “you must put all the parts together to find out what an elephant is like.”¹

Research on different aspects of shareholder litigation reflects a similar pattern. Many scholars have studied particular aspects of such litigation and the costs associated with that piece, but invariably without taking into account other pieces. Each is right, but only about the piece being described. For example, recent literature on shareholder litigation includes articles about derivative suits in federal courts,² class action litigation in state courts,³ and competition between courts,⁴ none of which fully takes

¹ This paragraph paraphrases the ancient fable. It is recounted in several forms, but this version is described in LILLIAN QUIGLEY, *THE BLIND MEN AND THE ELEPHANT* 24 (1959).

² See, e.g., Jessica Erickson, *Corporate Governance in the Courtroom: An Empirical Analysis*, 51 WM. & MARY L. REV. 1749 (2010) (providing an empirical examination of shareholder derivative suits in the federal courts).

³ See, e.g., Jennifer J. Johnson, *Securities Class Actions in State Court*, 80 U. CIN. L. REV. 349 (2012) (evaluating the impact of Congressional preemption and preclusion upon state court securities class actions).

into account findings in adjacent areas.⁵ To be truly effective, however, corporate law scholarship needs to give a picture of the whole beast and not just some of its parts.

In this Article, we begin by briefly revisiting the important role of shareholder litigation in controlling opportunistic managerial behavior and reducing managerial agency costs. With this background, we develop a theory of shareholder litigation occurring in corporate and securities laws, and describe how it changes over time. We then apply our theory to analyze multijurisdictional litigation in shareholder lawsuits to explain that phenomenon and the concerns it raises. Finally, we propose possible policy solutions addressing those concerns.

Our theory is based on two core characteristics that shape shareholder litigation. First, shareholders' power to sue, along with their related powers to vote and sell, derive from different national and state laws, which create multiple sources for the substantive legal rules. Over time, the strength of particular legal rules ebbs and flows as statutes, court rulings, and economic contexts change. In response, shareholders adjust their preferred approaches seeking to constrain managerial opportunism, including shifting litigation from one jurisdiction to another. Importantly from our perspective, these movements are dynamic and provide constantly changing arbitrage opportunities.

The second core characteristic is that representative litigation necessarily involves self-designated agents speaking for a collective group and multiple agents competing for the coveted spokesperson role. In the corporate context, representative litigation includes traditional derivative suits brought by a single shareholder in the name of the entity and class actions brought by one shareholder on behalf of a class of shareholders. In such claims, plaintiffs' lawyers typically have a greater economic stake in the litigation than the individual representative shareholder, so litigation agency costs may ensue.

⁴ See, e.g., John Armour, Bernard Black & Brian Cheffins, *Delaware's Balancing Act*, 87 IND. L.J. 1345 (2012) [hereinafter *Delaware Balancing*] (examining the implications of a sharp drop in Delaware's popularity as a venue for corporate litigation); John Armour, Bernard Black & Brian Cheffins, *Is Delaware Losing Its Cases?*, 9 J. EMPIRICAL LEGAL STUD. 605 (forthcoming 2012) [hereinafter *Delaware Cases*] (presenting evidence that corporate lawsuits against Delaware companies are increasingly brought outside Delaware); Brian JM Quinn, *Shareholder Lawsuits, Status Quo Bias, and Adoption of the Exclusive Forum Provision*, 45 U.C. DAVIS L. REV. 137 (2011) (arguing that behavioral economics can provide insight as to why few incorporators contract around default rules and adopt innovative self-help provisions).

⁵ We have contributed to these studies. See Robert B. Thompson & Randall S. Thomas, *The New Look of Shareholder Litigation: Acquisition-Oriented Class Actions*, 57 VAND. L. REV. 133 (2004) [hereinafter *New Look*]; Robert B. Thompson & Randall S. Thomas, *The Public and Private Faces of Derivative Lawsuits*, 57 VAND. L. REV. 1747 (2004) [hereinafter *Derivative Lawsuits*]. Our more recent work takes a more global view by looking at all litigation arising from mergers over a two-year period. See C.N.V. Krishnan et al., *Shareholder Litigation in Mergers and Acquisitions* (Georgetown Law & Econ. Research, Working Paper No. 11-23, 2012), available at <http://ssrn.com/abstract=1722227> [hereinafter *Litigation in Mergers*].

To understand how shareholders enforce their litigation and other rights, one must understand the principal-agent relationships that underlie those rights. These relationships change over time, making it important to examine them in their historical context. Our theory, which is based on these characteristics, explains the various forms of representative litigation and how they each change over time. It also illuminates the reasons for the rise and fall of different types of litigation at particular times. Applying our theory, we predict that: (1) the relative strength of the different forms of shareholder litigation will shift over time, (2) these shifts can result in new avenues for the expression of shareholder litigation power, (3) new agents will emerge to act on shareholders' behalf when these shifts occur (or old agents will put on new hats), and (4) a new set of principal-agent costs resulting from litigation will arise out of these new relationships, leading to recurrent questions about how to best control these costs in particular contexts. The resulting variations lead to changes in management agency costs, litigation agency costs, or both.

More broadly, this is a story of choice: first among the various legal avenues available to shareholders seeking to check the broad powers that law provides to managers in corporations, second among the different litigants and law firms seeking to bring or defend litigation, and third among the courts in the various jurisdictions in which the suits are brought. Litigation is an important managerial agency-cost-reduction device for shareholders, but they have other mechanisms as well, such as voting their shares and selling their stock. The relative strength of each of these monitoring devices changes over time, and the interaction of the three affects the litigation pattern that we see. There are dynamic changes in the strength of each of these monitoring devices, and these changes interact with litigation in important ways.

Derivative suits were the dominant form of shareholder litigation for most of the twentieth century. Concern about "strike suits"⁶ led to new laws in the middle part of the century, requiring bonds and later demand upon directors as a condition for bringing suits.⁷ Over time, shareholders brought more corporate governance litigation in federal court under Rule 10b-5 in order to avoid state law roadblocks and to benefit from the substantive interpretations of federal securities laws that, for a time, were favorable for such claims.⁸ Such action resulted in a surge of federal securities class actions and the perception that more frivolous cases were being filed too

⁶ The term "strike suits" describes suits "brought not to redress real wrongs, but to realize upon their nuisance value." *Cohen v. Beneficial Indus. Loan Corp.*, 337 U.S. 541, 548 (1949) (noting that derivative suits have long been "the chief regulator of corporate management").

⁷ See *New Look*, *supra* note 5, at 149-50 (discussing strike suits, bond requirements, and demand).

⁸ See *Basic Inc. v. Levinson*, 485 U.S. 224, 245-46 (1988) (applying a presumption of reliance in a fraud on the market context, facilitating filings of class action suits in a Rule 10b-5 context).

quickly while meritorious cases settled too cheaply.⁹ This set the stage for passage of the Private Securities Litigation Reform Act (PSLRA), which mandated new methods to determine lead plaintiffs and their lawyers, modified rules for pleading fraud, and imposed new constraints on settlements and attorneys' fees.¹⁰ A subsequent flow of securities class actions to state court led to additional federal legislation banning state court jurisdiction over such claims.¹¹

Around the same time, Delaware decisions facilitated merger-related class actions, a context not covered by the new federal laws.¹² Agents adapted to represent shareholder interests in this new forum, and legal rules evolved to address agency costs such as judges' efforts to cabin what they saw as excessive fees in representative litigation to impose new rules for determining lead plaintiffs.

In Part II, we apply our theory to address an element of corporate litigation generating current scholarly and practice-oriented discussions: allegations of forum shopping in corporate litigation in which simultaneous claims are brought in multiple jurisdictions, allegedly for the purpose of securing advantages unrelated to the substance of the claim. We first review the arguments for and against forum shopping as a general practice and show that recent increases in multijurisdictional litigation are largely not forum shopping in the traditional sense. Rather, the pattern is that some plaintiffs' law firms file these cases in an effort to obtain a slice of the attorneys' fees awarded in representative litigation cases that settle. We call this "fee distribution litigation" because these lawyers attempt to derive economic rents by manipulating the jurisdictional and venue rules in which litigation occurs, as distinguished from adding value through their litigation efforts.

We then move on to assess the best methods to control and limit fee distribution litigation. These include judicial solutions, such as increased comity and cooperation, and potential legislative solutions, including the federalization of litigation over acquisition-oriented class actions and coordinated state legislation. We finish with a survey of the private ordering solutions, including proposals for charter and bylaw amendments. We

⁹ See, e.g., John W. Avery, *Securities Litigation Reform: The Long and Winding Road to the Private Securities Litigation Reform Act of 1995*, 51 BUS. LAW. 335, 336 (1996) ("[T]he original focus of the [PSLRA] reform debate was a concern in Congress that there had been an explosion of meritless securities lawsuits, particularly class actions, filed solely for their settlement value . . ."); Elliott J. Weiss & John S. Beckerman, *Let the Money Do the Monitoring: How Institutional Investors Can Reduce Agency Costs in Securities Class Actions*, 104 YALE L.J. 2053, 2060–64 (1995) (discussing practices prior to the PSLRA).

¹⁰ See Private Securities Litigation Reform Act of 1995, Pub. L. No. 104-67, 109 Stat. 737 (codified as amended in scattered sections of 15 U.S.C.).

¹¹ See Securities Litigation Uniform Standards Act (SLUSA) of 1998, Pub. L. No. 105-353, 112 Stat. 3227 (codified as amended in scattered sections of 15 U.S.C.).

¹² See *New Look*, *supra* note 5, at 135.

conclude that none of the proposed solutions will eradicate fee distribution litigation. However, when we balance the need to control managerial agency costs with the litigation agency costs generated by this form of multijurisdictional litigation, we conclude that judicial comity is the most promising and also one of the easiest approaches to implement.

I. SHAREHOLDER LITIGATION AND OTHER LIMITS ON MANAGEMENT POWER

Law places corporate power in a centralized, hierarchical form that management dominates.¹³ There are both efficiencies to such specialization of function and also concerns that managers' self-interest can depart from the interests of those whose money is at risk. Various market characteristics, contractual rights, and legal rules interact to constrain such authority. Within corporate law, three limited powers are given to shareholders: they can sell their stock, they can vote their shares, or they can sue to enforce fiduciary duties or other obligations of officers and directors.¹⁴

Our focus here is on the litigation power. We develop a theory to describe the various alternatives for representative litigation, the costs and benefits of each, and the dynamic flow of litigation among various available alternatives. But the two other shareholder powers—to vote or to sell—present parallel dynamics. Each can serve as a limit on centralized corporate power, and if one avenue closes, shareholders and their agents will gravitate to another. Any complete understanding of corporate governance must take into account the substitution possibilities of the various remedies available to shareholders, the incentives of the multiple players to move between these remedies, and how that movement shapes new developments. The dual sources of these rights in federal and state law limit the likelihood that law will ever provide a single, uniform approach to addressing management agency costs.

The interaction of the poison pill,¹⁵ shareholder voting, and shareholder litigation provides a good example of this substitution dynamic. As lawyers developed—and judges approved—management's use of poison pills, this innovative defensive tactic made acquiring control via purchase of shares in a tender offer too expensive.¹⁶ A bidder's effort to prevail in a hostile

¹³ See DEL. CODE ANN. tit. 8, § 141(a) (2011); MODEL BUS. CORP. ACT § 8.01(b) (2011).

¹⁴ See Robert B. Thompson, *Preemption and Federalism in Corporate Governance: Protecting Shareholder Rights to Vote, Sell, and Sue*, 62 LAW & CONTEMP. PROBS. 215, 216 (1999).

¹⁵ The poison pill is a director-implemented plan of a target corporation to make a hostile tender offer prohibitively expensive to the bidder by providing all other shareholders other than the hostile bidder with a right to buy new shares at half price. The practical effect is to close off shareholders' ability to constrain management via selling shares by removing the bidder willing to buy those shares. See ROBERT B. THOMPSON, *MERGERS AND ACQUISITIONS: LAW AND FINANCE* 77 (2010).

¹⁶ The Delaware Supreme Court approved a board's authorization of the poison pill in *Moran v. Household Int'l, Inc.*, 500 A.2d 1346, 1351 (Del. 1985) (“[O]ur corporate law is not static. It must grow

takeover came to depend on persuading holders to vote their shares for a takeover, rather than persuading shareholders to sell their stock in a tender offer.¹⁷ In other words, as selling became a less effective form of monitoring corporate management, shareholders' focus shifted to voting activities. Litigation patterns also changed as the poison pill and other defenses gave target directors more time to stop hostile takeovers. Litigation based on federal tender offer legislation¹⁸—which largely had been used to delay bidders—decreased, and claims arising under state law duties set out in *Unocal Corp. v. Mesa Petroleum Inc.* and *Revlon Inc. v. MacAndrews & Forbes Holdings, Inc.*, which invited closer judicial scrutiny of the substance of takeover defenses, took on more importance.¹⁹

A second substitution example illustrates the interaction of voting and selling, specifically in the context of classified boards as a takeover defense under Delaware law.²⁰ A Delaware statute authorizes classified boards,²¹ and the state's supreme court has been generous in permitting companies to use the combination of classified board provisions and poison pills to effectively block shareholders' ability to sell their shares.²² In response,

and develop in response to, indeed in anticipation of, evolving concepts and needs." (alteration in original) (quoting *Unocal Corp. v. Mesa Petroleum Co.*, 493 A.2d 946, 957 (Del. 1985)). The *Moran* opinion concluded with a statement that the board's obligation to redeem a poison pill would be subject to judicial review, leaving open a check from the court. *Id.* at 1357. Within a few years, subsequent decisions seemed to make clear that the Delaware Supreme Court would be reluctant to use such authority. See *Paramount Commc'ns, Inc. v. Time Inc.*, 571 A.2d 1140, 1152–53 (Del. 1989) (overruling the earlier chancery court decision in *City Capital Associates Ltd. Partnership v. Interco Inc.*, 551 A.2d 787 (Del. Ch. 1988), that had forced a board to redeem a poison pill).

¹⁷ The Delaware Supreme Court's embrace in *Paramount* of the target directors' decision to "just say no" to a request to redeem the poison pill led bidders to launch a proxy contest to elect new members to the board who would exercise the redemption rights in the pill, which in turn led to target defensive tactics aimed at closing off the voting channel and Delaware decisions addressing shareholder voting rights. See *Air Prods. & Chems., Inc. v. Airgas, Inc.*, 16 A.3d 48, 113–19 (Del. Ch. 2011) (discussing when a defensive response makes a bidder's ability to wage a successful proxy contest and gain control of the target's board realistically unattainable).

¹⁸ In 1968, Congress added §§ 13d and 14d–f to the Securities Exchange Act of 1934, providing for disclosure and other substantive regulation of tender offers. See Act Providing for Full Disclosure of Corporate Equity Ownership of Securities Under the Securities Exchange Act of 1934, Pub. L. No. 90-439, 82 Stat. 454 (1968) (codified in relevant parts at 15 U.S.C. § 78m(d), n(d)–(f)).

¹⁹ See *Revlon, Inc. v. MacAndrews & Forbes Holdings, Inc.*, 506 A.2d 173, 182 (Del. 1986) (directors' duty in a takeover shifts to getting the best price for shareholders upon directors' decision to break up the company or put it up for sale); *Unocal*, 493 A.2d at 955 (defensive tactics in a takeover trigger intermediate judicial review where the board is required to show a threat and a proportional response).

²⁰ In "classified boards" with three classes, like in the U.S. Senate, only one-third of the seats turn over at any one annual meeting, so that a hostile bidder seeking to acquire control of the majority of the board, so as to direct the corporation, would need to wage proxy contests at two annual meetings.

²¹ See DEL. CODE ANN. tit. 8, § 141(d) (2011).

²² See *Versata Enters. v. Selectica, Inc.*, 5 A.3d 586, 604 (Del. 2010) ("The fact that a combination of defensive measures makes it more difficult for an acquirer to obtain control of a board does not make such measures realistically unattainable, i.e., preclusive."); Paul H. Edelman & Randall S. Thomas, *Selectica Resets the Trigger on the Poison Pill: Where Should the Delaware Courts Go Next?*, 87 IND. L.J. 1087 (2012).

institutional shareholders have turned from litigation to voting to protect their assets. Their strategy is to make shareholder proposals under Rule 14a-8 of the federal securities law to recommend deletion of classified voting provisions in corporate charters and to threaten to vote against directors who do not implement such recommendations.²³ This strategy has resulted in a remarkable shift in the governance structure of large American corporations, which have largely abandoned classified boards in recent years.²⁴

The larger space for voting rights also illustrates the important and sometimes distorting role of shareholders' agents in the exercise of alternative constraints; this role parallels traditional concerns expressed about plaintiffs' law firms in the exercise of shareholder litigation rights.²⁵ A pronounced change in the shareholder census over the last half century shows a sharp movement toward greater ownership of shares through intermediaries such as retirement funds or mutual funds. These intermediaries have looked to a second set of agents, proxy voting advisors, to determine how these funds should exercise voting rights.²⁶ In turn, there has been a growing concern over agency costs associated with proxy voting advisors and the potential distortion of voting rights by intermediaries and their agents.²⁷

While we see room to expand our analysis to include other forms of shareholder power, such as voting and selling, this Article focuses on litigation. However, we note that our theory could be used to explain selection among different forms of shareholder power, as they illustrate the same dynamic changes that we describe here with litigation.

²³ See 17 C.F.R. § 240.14a-8 (2011) (proxy regulation permitting shareholders to include proposals on a company's proxy).

²⁴ See TED ALLEN ET AL., INSTITUTIONAL S'HOLDER SERVS., PRELIMINARY 2011 U.S. POSTSEASON REPORT 6-7 (2011), available at <http://www.issgovernance.com/docs/2011USSeasonPreview> (reporting that shareholder support for board declassification proposals reached new highs, and the percentage of S&P 500 firms with classified boards dropped significantly in recent years); see also Randall S. Thomas & James F. Cotter, *Shareholder Proposals in the New Millennium: Shareholder Support, Board Response, and Market Reaction*, 13 J. CORP. FIN. 368, 389 (2007) (arguing that boards are increasingly willing to remove the classified board structure in response to shareholders' requests).

²⁵ See Yin Wilczek, *SEC Moving Soon to Address Proxy Advisory Firms*, *Official Says*, 43 SEC. REG. & L. REP. 2354, 2354 (Nov. 21, 2011) (reporting remarks by Meredith Cross, SEC Director, Division of Corporate Finance, made on November 10, 2011).

²⁶ See James Cotter et al., *ISS Recommendations and Mutual Fund Voting on Proxy Proposals*, 55 VILL. L. REV. 1, 32 (2010) (charting the effect of Institutional Shareholder Services' (ISS) voting recommendations on shareholder and mutual fund voting).

²⁷ See Stephen Choi et al., *The Power of Proxy Advisors: Myth or Reality?*, 59 EMORY L.J. 869, 878 (2010); Randall S. Thomas et al., *Dodd-Frank's Say on Pay: Will It Lead to a Greater Role for Shareholders in Corporate Governance?*, 97 CORNELL L. REV. 1213 (2012).

A. Underlying Factors that Explain the Frequency and Form of Representative Litigation in Corporate and Securities Law

Shareholder representative litigation is different from other forms of representative litigation in large part because of its managerial agency-cost-reduction characteristics. Representative suits including the classics—*Smith v. Van Gorkom*,²⁸ *Weinberger v. UOP, Inc.*,²⁹ and more recently, *In re Southern Peru Copper Corp. Shareholder Derivative Litigation*³⁰ and *In re Del Monte Foods Co. Shareholders Litigation*³¹—illustrate the incredible importance of corporate representative litigation in this capacity. Liability rules and legal norms have been shaped and formed in large part through the holdings in these and other similarly significant class actions and derivative lawsuits. In this section, we focus on the three main types of shareholder representative suits currently visible in corporate and securities litigation: federal class actions that stem from allegations of fraudulent misstatements and omissions, class actions arising out of mergers and acquisitions, and derivative lawsuits claiming that a company’s officer or director has caused the company harm in violation of the agent’s fiduciary duty of loyalty.

Here, we identify the two core characteristics of shareholder litigation that are relevant to our approach. First, litigation rights in corporate and securities law arise from multiple independent legal sources in state and national law. Our federal system produces separate and distinct systems of state corporation law and federal securities laws, which are created and enforced by different parts of our government. These disparate parts generally work separately and independently of one another, subject to the Supremacy Clause and other rules of our constitutional system.³² The respective strength and practical importance of federal and state laws vary

²⁸ 488 A.2d 858 (Del. 1985) (plaintiff, as representative for class of shareholders, alleged harm when directors agreed to merger in grossly negligent manner).

²⁹ 457 A.2d 701 (Del. 1983) (plaintiff, as representative for class of minority shareholders, forced out of corporation via a cash-out merger on terms picked by the majority shareholder).

³⁰ C.A. No. 961-CS, 2011 WL 6440761, at *43 (Del. Ch. Dec. 20, 2011) (class action alleging that the corporation overpaid in purchasing a company from its controlling shareholder, leading to a \$1.35 billion judgment (plus pre-and post-judgment interest) for breach of fiduciary duty of loyalty), *vacated with order to parties to submit revised final order*, C.A. No. 961-CS, 2011 WL 6476919 (Del. Ch. Dec. 22, 2011). The Delaware Supreme Court affirmed the Chancery Court’s judgment (including \$304 million in attorneys’ fees). *See Ams. Mining Corp. v. Theriault*, Nos. 29, 2012, 30, 2012, 2012 WL 4335192 (Del Aug. 27, 2012).

³¹ 25 A.3d 813 (Del. Ch. 2011) (class action leading to a temporary injunction of a shareholder vote on a buyout supported by management, as well as an injunction of the enforcement of defensive tactics under the merger agreement).

³² *See* U.S. CONST. art. VI, cl. 2. State law must yield to conflicting federal rules, but Congress has chosen not to supplant the general roles of incorporation found in state law, while still providing federal securities law that can provide specific obligations to control managers’ behavior. *See generally supra* notes 8–11 (citing major federal securities legislation).

over time.³³ The current state of our federalism suggests that these variations will continue in the future, and as they do, parties will continue to seek gains by choosing among the possible venues and types of claims.

Second, agency costs matter and arise in different ways depending on the form of litigation. In addition to the managerial agency costs discussed above, litigation can lead to agency costs as well. Shareholder suits under both state and national law are most frequently representative, meaning that the typical case involves one named plaintiff and, importantly, one or more law firms for that prospective representative seeking to speak for a large body of shareholders.³⁴ This can lead to litigation agency costs, for example, if agents bring what are perceived as strike suits or settle meritorious suits too cheaply. As new forms of representative litigation develop, new agency costs will accompany them. As a result, plaintiffs' law firms will migrate to newer, more fertile areas for litigation.

The last subpart of this section seeks to outline how the incentives of three major players—plaintiffs' law firms, defendants' law firms, and the courts—can be understood given the core factors we just described. Plaintiffs' law firms and their clients have an incentive to take advantage of substantive differences in law among jurisdictions and to improve a particular law firm's standing in the litigation and its share of any attorneys' fees that may follow. Defendants' law firms and their clients care about getting all the lawsuits arising out of a particular transaction dismissed in one swoop, but their position in obtaining a favorable settlement can be enhanced if the defendant can play one set of plaintiffs and law firms against another, in what has been termed a reverse auction.³⁵ Courts are the third set of players. Some commentators have argued that states do not compete for incorporation in terms of the long-debated race to the bottom or the top, but rather that state courts compete to attract litigation.³⁶ Such competition takes multiple forms, including, for example, varying judicial attitudes toward awarding plaintiffs' attorneys' fees.³⁷

³³ Since 1995, major federal legislation includes the PSLRA, SLUSA, and the subsequent enactment of the Sarbanes–Oxley and the Dodd–Frank legislation. *See supra* notes 8–11.

³⁴ *See* Roberta Romano, *The Shareholder Suit: Litigation Without Foundation?*, 7 J.L. ECON. & ORG. 55, 55–56 (1991) (noting argument of critics of shareholder suits that the plaintiffs' bar is the true beneficiary of the litigation).

³⁵ *See infra* text accompanying note 257 (discussing reverse auctions).

³⁶ *See* Matthew D. Cain & Steven M. Davidoff, *A Great Game: The Dynamics of State Competition and Litigation* 7–8, 31 (Apr. 1, 2012) (unpublished manuscript), available at <http://ssrn.com/abstract=1984758>.

³⁷ *See id.* at 5 (finding that some states, such as Delaware, California, Tennessee, Nevada, and Georgia, award significantly higher attorneys' fees than other states, including New Jersey, Illinois, and Massachusetts); *see, e.g., Delaware Balancing, supra* note 4, at 49–50 (discussing possible Delaware strategy to halt the outward migration of Delaware cases).

1. *Multiple Shifting Sources of Substantive Legal Rules Regulating Corporate Manager Behavior Open New Avenues for Litigation.*—Substantive legal rules that constrain the behavior of those given the authority to control our largest corporations are found in both state and federal law. State corporation law defines the authority of managers, directors, and shareholders.³⁸ Its rules—that directors can speak for the corporation on all corporate actions and can delegate their authority to managers—are the accepted starting points in both state and federal law.³⁹ The multiple state and federal laws provide different, and not necessarily overlapping, methods to constrain these broad powers.

State law has long been a principal source of challenge to the misuse of corporate power, particularly where states impose fiduciary duties of care and loyalty upon those who control corporations.⁴⁰ Federal securities laws, and in particular, the antifraud prohibition found in Rule 10b-5, provide a cause of action for misleading statements or omissions in connection with the purchase or sale of securities.⁴¹ Many corporate complaints have elements of both breach of fiduciary duty and fraud, so substitution of one kind of litigation for another is a recurring possibility, even as the reach of each law and its perceived utility changes over time.⁴² For example, Delaware became a more attractive litigation venue when, in the 1980s, its supreme court expanded the space for class actions in the context of mergers.⁴³ In federal law, an expansive period in the construction of Rule 10b-5 as applied to corporate governance issues was followed by a period of retrenchment.⁴⁴ Over time, federal securities law has broadened to take in more and more of corporate internal affairs,⁴⁵ so that more behavior is covered by the two overlapping systems, and participants may be able to pursue one action instead of another for strategic reasons.

Within this dual federal–state system, and a state system with more than fifty jurisdictions, procedural and jurisdictional rules make it possible to file suits in multiple jurisdictions arising from the same act, even if each

³⁸ See, e.g., MODEL BUS. CORP. ACT chs. 7–8 (2011) (naming shareholders, directors, and officers, respectively, as participants in a corporation and defining their core roles). More than half of the states have used the Model Business Corporation Act (MBCA) as the format for their act. See 1 MODEL BUS. CORP. ACT ANN., at ix (4th ed. 2008 & Supp. 2011) (listing thirty-one states as adopting all or substantially all of the MBCA as their general corporation statute).

³⁹ See, e.g., MODEL BUS. CORP. ACT § 8.01(b).

⁴⁰ See *New Look*, *supra* note 5, at 135–36.

⁴¹ 17 C.F.R. § 240.10b-5 (2011).

⁴² See Robert B. Thompson & Hillary A. Sale, *Securities Fraud as Corporate Governance: Reflections Upon Federalism*, 56 VAND. L. REV. 859, 904 (2003).

⁴³ See *Weinberger v. UOP, Inc.*, 457 A.2d 701, 703 (Del. 1983).

⁴⁴ See *Santa Fe Indus., Inc. v. Green*, 430 U.S. 462, 474 (1977) (breach of fiduciary duty without any deception, material misrepresentation, or nondisclosure did not violate the Securities Exchange Act).

⁴⁵ See Thompson & Sale, *supra* note 42, at 904 (discussing spread of federal law to legal obligations of officers and managers).

jurisdiction applies the same substantive law. This creates the possibility of multiple filings in shareholder litigation. Thus, the general jurisdiction that states provide to one or more of their courts, and judicial precedent that frowns on one state limiting the jurisdiction of another, means a plaintiff may sue directors in the corporation's state of incorporation, or alternatively, in the state where the corporation is headquartered (assuming the defendants have the necessary presence in the jurisdiction). Alternatively, many federal rights can be enforced in state courts,⁴⁶ and state rights may, in some cases, be brought in federal court.⁴⁷

Over the last two decades, significant statutory changes have altered this landscape. First, federal statutes preempted many state substantive claims in the securities area.⁴⁸ In addition, there has been some expansion of the ability of federal courts to hear substantive claims arising under state law.⁴⁹ These changes, while notable and sometimes complex, are incomplete. That incompleteness leaves open opportunities for multiple plaintiffs, and the law firms representing them, to file representative litigation while widening the array of policy issues to consider in determining society's proper response.

2. *Characteristics of Representative Litigation that Contribute to Multiple Suits.*—Representative litigation is different from what might be termed ordinary corporate litigation, in which centralized management speaks for the entity in litigation against an outside party.⁵⁰ In representative cases, an individual shareholder files suit on behalf of a large group, either the entire corporation, as in the case of a derivative claim, a class of shareholders affected by a change-of-control transaction (deal

⁴⁶ This is true, for example, of rights under the Securities Act of 1933, 15 U.S.C. § 77v(a) (2006) (concurrent jurisdiction in state courts for violations of the Securities Act except as to covered securities), but not of the Securities Exchange Act of 1934, 15 U.S.C. § 78aa (exclusive jurisdiction in federal courts for violations of the Securities Exchange Act).

⁴⁷ U.S. CONST. art. III, § 2 (judicial power of the federal courts shall extend to controversies between citizens of different states). This diversity jurisdiction is provided to prevent bias against an out-of-state plaintiff by permitting state claims to be heard in federal court when the parties are from different states.

⁴⁸ See, e.g., National Securities Markets Improvement Act of 1996, Pub. L. No. 104-290, 110 Stat. 3416 (codified as amended at 15 U.S.C. § 77r) (preempting a long-standing state law regulation of registration of securities issuance as to covered securities, such as those of the companies listed on a national stock exchange); Securities Litigation Uniform Standards Act of 1998, Pub. L. No. 105-353, 112 Stat. 3227 (codified in scattered sections of 15 U.S.C.) (banning securities class actions arising under state securities laws that had predated and paralleled portions of the federal securities laws).

⁴⁹ See Class Action Fairness Act of 2005, Pub. L. 109-2, 119 Stat. 4 (codified as 28 U.S.C. §§ 1332(d), 1453, 1711–1715 (2006)) (broadening the diversity principle to assure a federal forum for nationwide class actions); see also Samuel Issacharoff & Richard A. Nagareda, *Class Settlements Under Attack*, 156 U. PA. L. REV. 1649, 1656 (2008) (the Class Action Fairness Act pulls “national-market cases into the federal judicial system,” which is thought to be “less susceptible to capture and more capable of remedying improper forum selection”).

⁵⁰ See, e.g., *Amanda Acquisition Corp. v. Universal Foods Corp.*, 877 F.2d 496 (7th Cir. 1989) (bidder, acting through its board of directors, brought suit against target company).

litigation), or on the market in a Rule 10b-5 suit alleging fraudulent misrepresentations. The usual economics of these suits are that the individual shareholder will not gain enough from a successful resolution of the claim to make it worthwhile to incur the costs that a suit would entail. Plaintiffs' lawyers step into this gap.⁵¹ The attorneys' fees that they are able to collect from the entire group make it worthwhile for them to incur substantial costs in pursuing the litigation; as such, they become the economic driver of the typical representative litigation.⁵² Further, multiple-plaintiff law firms can compete to be the class representative, and multiple lawsuits, including in different jurisdictions, can be an effective way to shift (or increase) attorneys' fees.

In such a setting, however, law firms may have incentives to file too quickly and too often, and to settle too cheaply.⁵³ These problems have triggered a series of legal reforms, for example: bond requirements for derivative suits during the 1940s;⁵⁴ demand requirements and special litigation committees in the 1980s;⁵⁵ and the PSLRA in 1995, which requires courts to appoint lead plaintiffs, imposes heightened pleading requirements for securities fraud class actions, and seeks to obtain more judicial sanctions of abusive litigation.⁵⁶

Most recently, commentators have pointed to a new form of litigation agency cost—widespread forum shopping by plaintiffs' law firms through the use of multijurisdictional representative litigation.⁵⁷ As evidence of such activity, they cite a significant increase in the percentage of mergers and acquisitions deals facing litigation.⁵⁸ Typically, suits will be filed in a state court in the state of incorporation, often the Delaware Court of Chancery, and a second set of almost identical actions will be filed in a state court where the company's corporate headquarters is located. Both cases arise out

⁵¹ See Romano, *supra* note 34, at 55 (“[T]he cost of bringing a lawsuit, while less than the shareholders’ aggregate gain, is typically greater than a shareholder-plaintiff’s pro rata benefit.”).

⁵² Plaintiffs’ lawyers are inclined to fill the gap and finance litigation because “[t]he fee awarded to class counsel, like the standard contingency fee, reflects payment for the lawyer’s assumption of risk and cost of financing the litigation, as well as payment for legal services.” Jill E. Fisch, *Lawyers on the Auction Block: Evaluating the Selection of Class Counsel by Auction*, 102 COLUM. L. REV. 650, 660 (2002).

⁵³ See *New Look*, *supra* note 5, at 152–57 (identifying indicia of litigation agency costs).

⁵⁴ See *id.* at 150.

⁵⁵ See *id.*

⁵⁶ See Stephen J. Choi & Robert B. Thompson, *Securities Litigation and Its Lawyers: Changes During the First Decade After the PSLRA*, 106 COLUM. L. REV. 1489, 1500, 1503, 1507 (2006).

⁵⁷ See e.g., Quinn *supra* note 4, at 155 (“The out-of-Delaware litigation strategy appears to be an effort by plaintiffs’ counsel to skirt attempts by the Delaware judiciary to more closely monitor agency costs associated with shareholder lawsuits.”).

⁵⁸ See sources cited *supra* note 4.

of the same transaction and make nearly identical claims under the law of the state of incorporation.⁵⁹

Undoubtedly, much of the impetus for multijurisdictional litigation in representative litigation is driven by the U.S. Supreme Court's decision in *Matsushita Electric Industrial Co. v. Epstein*.⁶⁰ There, the Court held that a broadly written settlement release in an action in one jurisdiction controlled settlements made later in other jurisdictions, creating big payoffs for the particular plaintiffs' firm in the settling jurisdiction, as well as providing a possible advantage to the defendants in settling the litigation with one class representative instead of another.⁶¹ In that case, Matsushita Electric Industrial Co. (Matsushita) agreed to buy MCA, Inc., resulting in two lawsuits brought on behalf of MCA shareholders. The first was a Delaware state court action alleging that the MCA directors violated their fiduciary duties to shareholders by failing to carry out a market check to meet fiduciary duties set out in *Revlon* to obtain the best price for shareholders.⁶² The second was a federal action alleging that the terms of the tender offer eventually agreed upon by the two managements involved MCA's CEO and COO receiving different consideration for their shares than other MCA shareholders, and therefore violated federal tender offer rules requiring that all shareholders receive the best price.⁶³ Parties to the Delaware litigation reached a settlement quickly, but the Delaware vice chancellor rejected the Matsushita settlement because of the absence of any monetary benefits to the class (while proposing a large attorneys' fees award) and because of the potential value of the federal claim that the settlement proposed to release.⁶⁴ A subsequent global settlement proposed in state court eventually obtained the Delaware court's approval after the defendants added \$2 million in cash for the shareholders, and a federal court granted the defendants' motion for summary judgment, which permitted the Delaware vice chancellor to

⁵⁹ See, e.g., *In re Allion Healthcare Inc. S'holders Litig.*, No. 5022-CC, 2011 WL 1135016 (Del. Ch. Mar. 29, 2011). In *In re Allion*, a New York complaint was filed two days after the announcement of a merger, followed by two Delaware complaints. The plaintiff in the second Delaware complaint then withdrew that complaint and refiled in New York, and that plaintiff then became co-lead plaintiff in the New York case. *Id.*

⁶⁰ 516 U.S. 367 (1996).

⁶¹ See discussion *infra* Part II.C.1.

⁶² *Matsushita*, 516 U.S. at 389-90 (Ginsburg, J., concurring in part and dissenting in part) (noting that the suit filed was in response to reports in the financial press that Matsushita was negotiating to buy MCA and that the complaint was amended after the federal suit was filed to include waste claims arising from the firm's exposure to tender offer liability).

⁶³ *Id.* at 370 (majority opinion). Although the Delaware complaint was amended to include a state law claim that the side deal was unfair, there was no federal securities claim made under the 1934 Exchange Act, as the federal courts have exclusive jurisdiction in adjudicating such claims. *Id.*

⁶⁴ *In re MCA, Inc. S'holders Litig.*, 598 A.2d 687, 689-90, 696 (Del. Ch. 1991) (noting that the state claim was extremely weak and that the only claim that had merit was the federal suit not asserted).

downgrade his prior estimate of the high value accorded to the possible federal suit.⁶⁵

Two years later, however, a federal appellate court reversed the district court and held that the Delaware settlement could not release Matsushita from liability on the federal claims.⁶⁶ The Supreme Court reversed, holding that the Delaware settlement was binding in all courts because of the Full Faith and Credit Act.⁶⁷ In a two-step analysis taken from *Marrese v. American Academy of Orthopaedic Surgeons*,⁶⁸ the Court determined first that Delaware law would give preclusive effect to the settlement, which would bar the federal claim from being litigated, and second that the securities laws did not repeal, either implicitly or explicitly, the Full Faith and Credit Act.⁶⁹

Matsushita has stimulated multijurisdictional litigation filings by plaintiffs' law firms by creating incentives for plaintiffs and their law firms left out of the litigation in the first court to seek a second court in which to file. Once they have established control over the case in the second court, they may be able to convince defendants to settle their action by offering to release claims made in both cases.

3. *Shareholder Litigation as Compared to Other Aggregate Litigation.*—Shareholder litigation as representative litigation has substantial commonalities with class actions generally, such that it shares similar concerns and responses. Yet, there are some significant differences in the corporate context. First, shareholder litigation plays a distinctive governance role as a key constraint on management agency costs, more specific than the compensatory and social welfare purposes of class actions. Second, representative litigation in a corporate context presents a different kind of risk. The Supreme Court has noted that “[t]here has been widespread recognition that litigation under Rule 10b-5 presents a danger of vexatiousness different in degree and in kind from that which accompanies litigation in general.”⁷⁰ Third, the governance overlay means that litigation procedures are intermixed with corporate governance issues, such as rules as to who can speak for the corporation and the ability of shareholders to contract about rules for making such a determination. Fourth, this corporate focus also generates a specific Delaware concern regarding control of its corporate law, which is seen as a valuable asset for that state.

⁶⁵ *In re MCA, Inc. S'holders Litig.*, No. 11,740 (Consolidated), 18 DEL. J. CORP. L. 1053 (Del. Ch. Feb. 12, 1993), *aff'd*, 633 A.2d 370 (Del. 1993) (unpublished table decision). The settlement fund for plaintiffs included attorneys' fees, which Vice Chancellor Hartnett cut to \$250,000. *Id.* at 1064.

⁶⁶ *Epstein v. MCA, Inc.*, 50 F.3d 644 (9th Cir. 1995), *rev'd sub nom. Matsushita Elec. Indus. Co. v. Epstein*, 516 U.S. 367 (1996).

⁶⁷ *Matsushita*, 516 U.S. at 373 (citing 28 U.S.C. § 1738 (1994)).

⁶⁸ 470 U.S. 373 (1985).

⁶⁹ *Matsushita*, 516 U.S. at 386.

⁷⁰ *Blue Chip Stamps v. Manor Drug Stores*, 421 U.S. 723, 739 (1975).

There are many areas in which issues raised in shareholder litigation parallel those in class actions more generally. Certainly class actions have social welfare and compensatory functions, and courts are sometimes portrayed as playing a fiduciary role.⁷¹ But at the same time, the specific characteristics of shareholder litigation generate distinctive responses, as reflected in the various legislative protections against abuse that have been implemented in the corporate and securities areas but not in class actions more generally.⁷²

4. *Understanding the Key Actors in Shareholder Litigation.*—As discussed above, the substantive and procedural laws governing representative litigation and the economic incentives they create increase the likelihood of multiple filings in shareholder litigation. To further illustrate why, and to frame the discussion of possible responses, we pause to focus separately on the roles of the three recurring players in the shareholder litigation context.

a. *Plaintiffs' law firm agency costs.*—Law firms, whose business plans are based on filing representative litigation on the plaintiffs' side, recognize that there is more than one possible representative for a shareholder group and that they likely will be competing with other plaintiffs' firms to become the lead lawyer. Barriers to entry in this field are fairly low. A law firm needs a client to file a suit, but in a publicly held corporation with widely dispersed shareholders, there are numerous possible clients. Even if another firm has already filed a lawsuit, there may be good economic reasons, from the law firm's standpoint, to file a second suit. A suit filed in another jurisdiction may bring into play substantive rights not covered in the first suit.⁷³ Filing a second suit in the same court may be advantageous if application of lead plaintiff provisions under federal securities law (or under some state laws) could result in the later-filing law firm being selected as class counsel. Alternatively, a law firm may file a second suit in order to get a seat at the settlement table and a claim to a share of the legal fees that may follow. Filing in another jurisdiction can also divert the main focus away from the first forum in favor of the new jurisdiction, and thereby allow a firm to claim control over the entire litigation.

These multijurisdictional filings are the inevitable result of the structure of the existing industry of plaintiffs' law firms in this area. Generally speaking, the larger, better funded firms will get the lead plaintiff

⁷¹ See Issacharoff & Nagareda, *supra* note 49, at 1707–08 (citing *Reynolds v. Beneficial Nat'l Bank*, 288 F.3d 277, 280 (7th Cir. 2002) (Posner, J.) (discussing courts as fiduciaries of class actions)).

⁷² See *supra* note 7 and accompanying text.

⁷³ See Jessica M. Erickson, *Overlitigating Corporate Fraud: An Empirical Examination*, 97 IOWA L. REV. 49, 70–71 (2011) (describing allegations against AIG alleging securities fraud in misleading the market, a derivative suit alleging conscious disregard of risk by directors, as well as separate ERISA and criminal suits).

role in federal securities suits, which are the most potentially remunerative. These firms are more likely to have developed relationships with the larger institutional clients who will be chosen as lead plaintiff.⁷⁴ These firms also will be more likely to handle (and if necessary finance) the more intense litigation.⁷⁵

Newer, smaller firms with fewer financial resources will only be able to enter the market if they find niches where they can litigate what they perceive as good cases without investing large amounts of resources but still earn sufficient fees to stay in business. Currently, multijurisdictional deal litigation is the best candidate for many of these firms because: (1) they can file these suits without making the type of investment necessary to overcome the difficult pleading hurdles imposed by the PSLRA in federal securities cases, (2) if they are shut out of the first-filed action in Delaware, or another state court, they can still file cheaply in either the state court of the target company's headquarters or in federal court, and (3) under *Matsushita*, if they can gain control of the litigation in whichever jurisdiction they file, they can offer to settle their case and get the entire matter dismissed. This creates substantial leverage with the other plaintiffs' law firms in competing cases in the event that the case settles with an attorneys' fee award.

Firms that spend substantial time and money to develop strong cases risk being undercut by competing firms that have filed and settled in other jurisdictions. Pressure from defendants' firms to get a global settlement of these cases,⁷⁶ and to make sure all the firms that have filed cases participate in the settlement, will lead to all of the plaintiffs' firms getting some slice of the fees awarded, cutting into the return of the firms that have done the larger amount of the work.

b. Defendants' firms' agency costs.—Defendants' firms, of course, have little say in where corporate suits are initially filed, although with federal cases they can enlist the Multidistrict Litigation (MDL) panel to transfer cases to a particular forum for pretrial proceedings.⁷⁷ In both

⁷⁴ See Neil Weinberg & Daniel Fisher, *The Class Action Industrial Complex*, FORBES, Sept. 20, 2004, at 150, 157.

⁷⁵ Well-established firms presumably have more resources, and to the extent that a firm must borrow from a bank to finance litigation, "only the long-established plaintiff's firms will be able to borrow based on future earnings, and newer firms will be limited to the debt level that the personal assets of their partners can collateralize." John C. Coffee, Jr., *Understanding the Plaintiff's Attorney: The Implications of Economic Theory for Private Enforcement of Law Through Class and Derivative Actions*, 86 COLUM. L. REV. 669, 706 n.104 (1986).

⁷⁶ Peter E. Kazanoff, *Multijurisdictional Shareholder Challenges to M&A Transactions*, in M&A LITIGATION 2011, at 39, 43 (Practising Law Institute 2011) [hereinafter M&A LITIGATION] ("[D]efense counsel almost always assert the 'all-we-care-about-is-one-forum position' . . ."). Failure to include any filing firm is likely to result in that firm objecting to the settlement and could potentially derail it.

⁷⁷ James D. Cox et al., *Do Differences in Pleading Standards Cause Forum Shopping in Securities Class Actions?: Doctrinal and Empirical Analyses*, 2009 WIS. L. REV. 421, 428–29.

federal and state courts, they can file a *forum non conveniens* motion to stay or dismiss the litigation on the grounds of an inconvenient forum.⁷⁸ However, the possibility of multiple suits and the incentives of plaintiffs' lawyers give defendants a powerful role in determining which suits are settled and an opportunity for defendants and their lawyers to play one plaintiff representative against another. Defendants have a strong preference for getting all suits dismissed. As such, they look for a means to get all plaintiffs involved in a global settlement. While defendants will generally prefer to litigate the Delaware action—because of the predictability of the decisions and attorneys' fees awards in that forum⁷⁹—and move to stay the litigation in other venues, there have been instances where they appear to have tried to settle weaker cases in other jurisdictions as a way of undercutting the stronger Delaware action.⁸⁰ Defendants can hold out the lure to several plaintiffs' firms of agreeing to a settlement with that plaintiff that would have preclusive effect under *Matsushita*, leading to the different plaintiffs competing for that result by offering settlement on terms favorable to the defendant in what has been called a reverse auction.⁸¹ Such a reverse auction may have several negative effects for shareholders, including good cases being dismissed or not prosecuted effectively, as the plaintiffs' firms filing them see their efforts as providing little or no benefit to them for the work provided. It may also encourage more multiple jurisdiction filings as some of those plaintiffs' law firms are rewarded for their forum choice. In short, defendants will try to reach global settlements of all cases arising out of the same transaction and may benefit from *Matsushita* by conducting reverse auctions in settlements.

c. Competition between courts.—Corporate law is full of debate about whether there is a race to the bottom or a race to the top among the states—a debate that has not been fully resolved, but one that, in any event, most academics believe Delaware has won.⁸² However, recently some commentators have argued that Delaware courts are competing for cases

⁷⁸ 28 U.S.C. § 1404 (2006) (*forum non conveniens*).

⁷⁹ While at first blush it seems odd that defendants would seek to litigate a good case in Delaware, remember that defendants' law firms are paid by the hour and therefore may be able to bill more time on a hard fought case. So long as the outcome is predictable, such a decision is likely to be in the best interests of their client as well.

⁸⁰ See, e.g., Transcript of Courtroom Status Conference, *Scully v. Nighthawk Radiology Holdings, Inc.*, No. 5890-VCL (Del. Ch. Dec. 17, 2010) (Laster, V.C.); Kazanoff, *supra* note 76, at 43 ("With plaintiffs in multiple jurisdictions, defense counsel charged with ensuring deal certainty may be motivated to negotiate and reach a settlement with plaintiffs' counsel who are the most willing to settle their claim and forgo a preliminary injunction hearing.")

⁸¹ See, e.g., John C. Coffee, Jr., *Class Wars: The Dilemma of the Mass Tort Class Action*, 95 COLUM. L. REV. 1343, 1370 (1995) [hereinafter *Class Wars*] (developing the concept of reverse auctions).

⁸² For a survey of some of the more recent literature, see ROBERTA ROMANO, FOUNDATIONS OF CORPORATE LAW 114–51 (2d ed. 2010).

with other courts,⁸³ and some go so far as to say that Delaware is losing.⁸⁴ These commentators argue that more and more corporate law cases are being filed outside of the Delaware courts because of a perceived anti-plaintiff bias, and that Delaware judges are trying various techniques to move them back to their courtrooms.⁸⁵ For example, Delaware awards fees that are on average \$400,000 to \$500,000 higher than other courts,⁸⁶ perhaps suggesting to plaintiffs that they do better there than elsewhere. Delaware judges gain prestige and influence from being the business court of the nation.⁸⁷ Delaware judges know that Delaware incorporations provide benefits to the state—15% to 20% of the state's budget arises from this sector, and its judges have a platform unmatched by other states.⁸⁸ However, competition may develop if judges in other state courts similarly want to be involved in high-profile corporate cases.

If such court competition exists, one would suspect that plaintiffs would select a forum based on the experience and knowledge of the judges, the predictability and speed of the decisions, and the perceived biases for or against plaintiffs. In these respects, the Delaware courts have a number of advantages. As the state of incorporation for the majority of the largest American corporations, Delaware has developed a judiciary focused on delivering a corporate law product.⁸⁹ Within the state, the jurisdiction of the court of chancery extends to all actions arising under the state's corporation law.⁹⁰ The court's five judges are repeat players in corporate law issues; 75% of their dockets arise from corporate law.⁹¹ These judges often have corporate law practice experience prior to appointment to the bench, and their steady diet of corporate law cases adds quickly to that background.⁹² In

⁸³ See Quinn, *supra* note 4, at 143; Faith Stevelman, *Regulatory Competition, Choice of Forum, and Delaware's Stake in Corporate Law*, 34 DEL. J. CORP. L. 57, 61 (2009).

⁸⁴ See generally *Delaware Cases*, *supra* note 4 (detailing the trend of filing suits outside of Delaware).

⁸⁵ See Cain & Davidoff, *supra* note 36, at 2 (describing attempts to attract corporate shareholder litigation to Delaware).

⁸⁶ *Id.* at 5.

⁸⁷ See Stevelman, *supra* note 83, at 98, 109 (noting Delaware judges' "effort to keep forum in high-profile Delaware corporate lawsuits").

⁸⁸ ROMANO, *supra* note 82, at 117.

⁸⁹ DEL. CODE. ANN. tit. 8, § 111(b) (2011).

⁹⁰ See *Delaware Balancing*, *supra* note 4, at 29–33 (discussing cases in which judges were sometimes critical of attorneys' fees); Cain & Davidoff, *supra* note 36 (discussing recent cases awarding large attorneys' fees).

⁹¹ See, e.g., *New Look*, *supra* note 5, at 165–66 (finding that about 75% of the civil actions filed in the New Castle County Chancery Court are classified as corporate matters).

⁹² For example, before becoming a judge, Chancellor Strine was a corporate litigator at Skadden, Arps, Slate, Meagher & Flom; Vice Chancellor Laster was a director in the corporate department of Richards, Layton & Finger and later formed the corporate boutique firm Abrams & Laster (later renamed Abrams & Bayliss); and Vice Chancellor Glasscock worked in the litigation department of Prickett, Jones & Elliott, a Delaware firm specializing in corporate work. See *Judicial Officers of the*

most other states, judges who hear corporate cases are based in courts of general jurisdiction whose dockets are filled with criminal law, family law, and other cases.⁹³

Another way courts could compete is based on speed of resolution. The chancery court has developed a commitment to expedited proceedings, which is shared by the Delaware Supreme Court, which hears any appeals.⁹⁴ This is important in deal cases because it gives the plaintiff an opportunity to seek an injunction to stop the deal from closing on a timely basis, or, at the very least, the opportunity to schedule such a hearing as leverage to force the defendants to settle and remove the threat of an injunction. Other courts must develop such policies too, or they will not effectively compete for cases.

In such court competitions, differences in particular procedural practices can provide some courts with advantages over others.⁹⁵ For example, if Delaware is not willing to schedule a preliminary injunction hearing in a merger case before the defendants have sent out a proxy statement to the target company's shareholders, other jurisdictions' courts may be willing to move forward without waiting. Similarly, if Delaware is normally unwilling to enjoin a transaction where no other bidder has come forward,⁹⁶ other jurisdictions could try to compete by offering such a possibility. Finally, courts that do not permit juries, such as the Delaware Chancery Court, may be less able to attract plaintiffs seeking to try the case, as they cannot offer a sympathetic jury in a court of equity.⁹⁷

A third factor that could cut either for or against Delaware is the predictability of the outcome on the merits of such cases; Delaware has a more experienced judiciary and much more developed precedent in corporate law than any other state. This may mean its law is more certain and judges are more likely to quickly grasp the main threads and the nuances of the questions at issue.

Court of Chancery, DELAWARE ST. CTS., <http://courts.state.de.us/chancery/judges.stm> (last visited Sept. 21, 2012).

⁹³ Some states have created special business courts, but those courts do not match Delaware in terms of the volume of cases or their sophistication.

⁹⁴ See Jill E. Fisch, *The Peculiar Role of the Delaware Courts in the Competition for Corporate Charters*, 68 U. CIN. L. REV. 1061, 1077 (2000) ("Delaware courts are also known for their ability to respond to business litigation quickly through, for example, granting expedited hearings and providing a rapid turnaround time on decisions.").

⁹⁵ Kazanoff, *supra* note 76, at 42–43 ("[L]iberal discovery rules in a particular jurisdiction may help shareholder plaintiffs leverage a settlement if the participants in the transaction become concerned that burdensome document requests, depositions, and other discovery will interfere with or delay the closing of a transaction.").

⁹⁶ See, e.g., *In re Del Monte Foods Co. S'holders Litig.*, 25 A.3d 813, 838 (Del. Ch. 2011) ("Absent an injunction, the Del Monte stockholders will be deprived forever of the opportunity to receive a pre-vote topping bid . . .").

⁹⁷ The absence of a substantial number of cases that actually go to trial mutes the impact of this factor.

Another factor is the judiciary's attitude toward these cases. Delaware judges may be overly concerned for corporations' welfare, according to some critics, which could hurt them in such a competition. However, a sympathetic hometown judge where the company is headquartered may act the same way if the deal at issue is likely to result in large-scale layoffs of employees or closing executive offices within the headquarters state.⁹⁸

In a related vein is a court's willingness to award attorneys' fees. At different times, Delaware judges have appeared to be more or less hostile to the size of attorneys' fees awards.⁹⁹ Chancery court judges do not give much deference to the parties' agreement on fee levels, which can lead to lower awards.¹⁰⁰ By comparison, other state courts may compete by acquiescing to the number agreed to by the defendants and plaintiffs.¹⁰¹ In sum, courts may compete to attract corporate litigation, and that can influence where cases get filed.

Finally, plaintiffs' law firms may believe that certain judges are more sympathetic to them than others. For example, an attorney that has clerked for a particular judge may think that this judge has a slight bias in his favor. Alternatively, an elected judge may be perceived to be beholden to major campaign contributors. While every court employs law clerks, not all judges are elected, including the judges on the Delaware Chancery Court, so this factor may lead to some cases being filed outside of Delaware.

B. Representative Litigation Today: Applying the Model to Understand Recent Patterns of Filing and Case Settlements

Representative litigation in the corporate and securities area is visible today in three prominent contexts. One context is class actions alleging fraudulent misstatements or omissions by companies to their shareholders in violation of federal securities laws. These class actions are sometimes paired with state derivative suits based on the same fact pattern, which allege breach of the directors' state law fiduciary duties.¹⁰² A second context presents as "deal" litigation, typically class actions challenging the terms of

⁹⁸ Kazanoff, *supra* note 76, at 42.

⁹⁹ See, e.g., Cain & Davidoff, *supra* note 36.

¹⁰⁰ See Pamela S. Tikellis, *Under the Microscope—Disclosure Based Settlements and Multijurisdictional Litigation*, in M&A LITIGATION, *supra* note 76, at 95, 97 (noting that the Delaware Chancery Court is reducing fee awards in disclosure-only settlements in recent years, even when the amount of the award is unopposed).

¹⁰¹ Kazanoff, *supra* note 76, at 43 ("By bringing a case in an alternative jurisdiction, plaintiffs may see an opportunity to obtain approval of a settlement—and a fee for their counsel—that might otherwise raise concerns in Delaware."); Charles M. Nathan, *Designating Delaware as the Exclusive Jurisdiction for Intra-Corporate Disputes*, in M&A LITIGATION, *supra* note 76, at 111, 113 (noting that plaintiffs' lawyers hope that "courts outside of Delaware are less likely to limit or reduce plaintiffs' attorneys' fee awards").

¹⁰² See generally Erickson, *supra* note 73 (detailing the parallel litigation that frequently occurs in instances of corporate fraud).

proposed or consummated acquisitions as breaches of fiduciary duties by management, directors, or both based on the law of the entity's state of incorporation. A third distinctive context, visible in contemporary litigation, is populated by traditional freestanding derivative suits (i.e., separate from securities class actions in our first category) that challenge the terms and conditions of interested transactions in which directors or officers have conflicts of interests or other purported breaches of fiduciary duties as determined by the corporations law of the issuer's state of incorporation. In this section, we lay out the main characteristics of each type of case as well as the factors leading to their being filed in multiple jurisdictions.¹⁰³

1. *Rule 10b-5 Class Actions with Tagalong Derivative Suits.*—Federal securities class actions alleging violations of Rule 10b-5 of the 1934 Exchange Act or similar provisions of the 1933 Securities Act remain the most visible form of shareholder litigation in corporate and securities law.¹⁰⁴ A corporate event producing an adverse market reaction regularly generates multiple suits; these suits allege failure to disclose information and seek to represent the class of shareholders who bought or sold after the nondisclosure.¹⁰⁵ Long-standing concerns about vexatious litigation have produced a variety of legislative “fixes” already mentioned.¹⁰⁶ The filing of these suits in federal courts has meant there are additional tools, such as the MDL panel provisions,¹⁰⁷ for dealing with multijurisdictional suits. An additional element of the multiplicity of filings, left relatively untouched by legislative reforms, occurs because these same factual contexts often generate shareholder derivative suits arising under state corporate law alleging breach of the directors' fiduciary duties. This provides a context to examine the extent to which the interaction of plaintiffs' law firms, defendants' law firms, and courts works to combat some of the problems arising from filings in multiple jurisdictions.

Since more than one person can claim to speak for the class, multiple suits are possible as different plaintiffs and law firms compete to speak for the group. Different procedural rules, however, have meant that the resolution of these multiple claims is a bit more orderly than the state law

¹⁰³ The material in this section is based on confidential conversations with judges, plaintiffs' lawyers, and defense counsel. These conversations were all undertaken with the understanding that the participants would not be identified and that none of their comments were for attribution. We have provided citations where there are published sources available.

¹⁰⁴ The Stanford Class Action Clearinghouse reports an average of 194 suits per year between 1997 and 2010. Press Release, Stanford Law School Class Action Clearinghouse, Securities Class Action Filings Increase Slightly in 2011, According to Report by Stanford Law School and Cornerstone Research (Jan. 19, 2012), available at http://securities.stanford.edu/scac_press/Cornerstone_Research_Filings_2011_YIR_Release.pdf; see also Cain & Davidoff, *supra* note 36, at 31 tbl.1 (reporting an average of about eighty transactions a year in the 2005–2010 period for litigation acquisitions).

¹⁰⁵ See 17 C.F.R. § 240.10b-5 (2011).

¹⁰⁶ See *supra* notes 48–49 and accompanying text.

¹⁰⁷ 28 U.S.C. § 1407 (2006) (providing for a panel on multidistrict litigation in federal courts).

class actions described below. Since 1995, federal law has provided a uniform way to pick a lead plaintiff among the various parties that would like to represent the class: the court selects a plaintiff, or group of plaintiffs, as lead plaintiff with the power to select a law firm or firms to represent the class; there is a presumption that the plaintiff with the largest financial stake should be named the lead plaintiff.¹⁰⁸ Federal procedural rules addressing multidistrict litigation further provide guidance in working out conflicts among multiple courts.¹⁰⁹ As a practical matter, these rules give the firms with the biggest clients and the most resources a significant advantage in obtaining the lead law firm positions in these cases. Law firms that did not—or could not—win the lead firm position are forced to look for alternative routes to participate.

In federal securities class actions, the losing plaintiffs' law firms—or those that lack the resources to litigate these relatively long and expensive cases—often file derivative suits arising out of the same underlying set of facts but alleging state law claims, such as breach of the duty to monitor, or a federal proxy fraud claim.¹¹⁰ Thus, a federal securities class action under Rule 10b-5 may allege that a company made material misrepresentations or omissions relating to a product development or securities issuance, causing an adverse effect on the company's stock price. The derivative suit in such a setting might allege that the company's directors breached their fiduciary duties in acting for the corporation, for example, by failing to meet their duty of care in regard to the conduct that generated the misleading disclosure.¹¹¹

These Rule 10b-5 suits, arising under federal securities law, can be brought in any federal district court where jurisdiction can be found, but are usually filed in the district where the company is headquartered.¹¹² The derivative suit's state law claims will be resolved under the law of the state of incorporation (i.e., Delaware for the majority of public corporations).¹¹³ While based on state substantive law, these derivative suits may be filed in the Delaware Chancery Court or in a state court in the headquarters state of

¹⁰⁸ 15 U.S.C. § 78u-4(a)(3) (2006) (governing the appointment of lead plaintiff).

¹⁰⁹ See 28 U.S.C. § 1407.

¹¹⁰ In recent years, there has been a proliferation of small plaintiffs' law firms that file such cases without competing in the lead plaintiff competition surrounding the class action. There are low barriers to entry in this type of litigation for these newcomers, as they do not actually engage in much litigation in the cases that they file. See Brian Cheffins et al., *Delaware Corporate Litigation and the Fragmentation of the Plaintiffs' Bar*, 2012 COLUM. BUS. L. REV. 427, 478 [hereinafter *Fragmentation*] (describing tagalong suits as attracting small firms that previously brought securities class action suits and switched to derivative suits).

¹¹¹ See Erickson, *supra* note 2, at 1756.

¹¹² Cain & Davidoff, *supra* note 36, at 31 (reporting only four cases outside of the headquarters jurisdiction or state of incorporation).

¹¹³ This is the internal affairs doctrine. See *CTS Corp. v. Dynamics Corp. of Am.*, 481 U.S. 69, 78 (1987); *VantagePoint Venture Partners 1996 v. Examen, Inc.*, 871 A.2d 1108, 1113 (Del. 2005); *In re The Topps Co. S'holders Litig.*, 924 A.2d 951, 953 (Del. Ch. 2007).

the company (which typically would have jurisdiction to hear a claim arising under the law of another state). An alternative, less favorable choice is to bring these state-law-based derivative cases in the same federal court as the Rule 10b-5 cases, relying on diversity jurisdiction.¹¹⁴ If they choose to file the state law claim in the same federal court hearing the Rule 10b-5 claim, the plaintiff and its law firm facilitate coordination of the cases for discovery and eventually for settlement.¹¹⁵

In settlement negotiations between the parties, these derivative suits are commonly settled with the federal class actions and are assigned a relatively small part of the value of any settlement funded by the directors' and officers' liability insurance (D&O) policy of the defendant firm.¹¹⁶ In some circumstances, the derivative claims may generate additional settlement funds based on payments made by the individual defendants, or more commonly they may permit the plaintiffs to obtain corporate governance changes at the defendant firms, a benefit that is not usually achievable in the class action.¹¹⁷ Moreover, these "tagalong" cases are almost never litigated actively on their own, as the state law claims are often weak ones and the procedural barriers that they face are quite high; they are generally filed after a securities class action and they rise or fall with the success of the federal class action.¹¹⁸

Securities class actions have been among the most studied forms of litigation in corporate and securities laws, particularly after the PSLRA introduced the problem of multiple litigations in the same court, which it resolved through the lead plaintiff provision already discussed.¹¹⁹ Our focus here is on a relatively less studied context: when federal securities class actions and state-law-based derivative suits are brought against the same company. Professor Jessica Erickson finds that in 75% of the derivative

¹¹⁴ Interview with plaintiffs' attorney (Jan. 31, 2012) (on file with authors) (The main problem for plaintiffs with filing the derivative suit in federal court is that the derivative suit will be stayed pending resolution of any motion to dismiss in the federal securities law class action. In some cases, a second wave of derivative suits will be filed in federal court after the resolution of the motion to dismiss in the Rule 10b-5 class action because if the court has ruled in the plaintiffs' favor, discovery will get underway.)

¹¹⁵ Researchers are much more able to locate the federal cases because the PACER electronic docket service is available for federal cases, whereas relatively few state courts have electronic filing and document systems at present. State court may have some advantages for the plaintiffs, as the discovery rules may be more favorable than in federal court.

¹¹⁶ For a discussion of the role of D&O insurance in the settlements of securities fraud class actions, see Tom Baker & Sean J. Griffith, *How the Merits Matter: Directors' and Officers' Insurance and Securities Settlements*, 157 U. PA. L. REV. 755, 796–804 (2009).

¹¹⁷ See Erickson, *supra* note 73, at 84–85 (discussing when derivative suits may be the only way to pursue legal redress).

¹¹⁸ See *id.* at 73 (comparing filing dates).

¹¹⁹ See Randall S. Thomas & Robert B. Thompson, *Empirical Studies of Representative Litigation*, in RESEARCH HANDBOOK ON THE ECONOMICS OF CORPORATE LAW 152 (Claire A. Hill & Brett H. McDonnell eds., 2012) (providing an overview of research regarding securities class actions).

cases there were also 10b-5 securities class actions.¹²⁰ These federal derivative suits are almost always filed in the federal district court where the headquarters of the company is located. For more than half of the companies, there is also a derivative case filed in a state court.¹²¹

Relevant to our discussion, 82% of the federal derivative claims are filed after the securities class action and state court derivative claims (hence the term tagalong).¹²² Erickson found that most of these cases produced nothing in the way of specific monetary recovery for the company; more than two-thirds were dismissed (as compared to 30% in overall federal litigation),¹²³ and only 2 of the 101 cases (exclusive of the backdating cases) produced any meaningful financial benefit for the company.¹²⁴ Nonmonetary relief was more common, and often came in the form of corporate governance changes, such as more independent directors or splitting the chief executive officer and chair of the board positions.¹²⁵ Having achieved such a result, which is not possible in the class action federal securities cases focusing on misstatements,¹²⁶ the derivative attorney enters into discussions as to how attorneys' fees should be shared.

Erickson finds that many of the same firms are repeat players in these derivative suits, which can be indicia of litigation agency costs in representative litigation.¹²⁷ Erickson also finds that the plaintiffs' lawyers who bring the federal derivative suits, while repeat players, tend to be a different group than those who bring the securities fraud class actions.¹²⁸ She suggests that the derivative claims are brought by plaintiffs' firms that are growing their way into a role in the bigger money securities class actions.¹²⁹

What are we to make of these findings? There clearly seems to be a large number of derivative cases based on the corporate law of the company's state of incorporation that are brought after a securities class action has been initiated. It is plausible that they result in additional nonmonetary benefits to shareholders. However, given that there is almost

¹²⁰ Erickson, *supra* note 73, at 62. This rises to more than 80% after the elimination of backdating cases. *Id.* at 62 n.54. Backdating cases are discussed in more detail *infra* Part I.B.3.

¹²¹ *Id.* at 65.

¹²² *Id.* at 72–73.

¹²³ Erickson, *supra* note 2, at 1794 (comparing to a study in two federal district courts).

¹²⁴ *Id.* at 1803.

¹²⁵ *Id.* (showing that corporate governance settlements are far more common for classic derivative suits). These corporate governance changes in some cases bear little relation to the wrong alleged, but they do count as a benefit to the corporation that can support an award of attorneys' fees.

¹²⁶ Class counsel is reluctant to seek corporate governance changes where they may result in a lower monetary recovery for the class.

¹²⁷ Erickson, *supra* note 2, at 1768–69.

¹²⁸ *Id.* at 1769; see generally *New Look*, *supra* note 5, 152–56 (describing indicia of litigation agency costs).

¹²⁹ Erickson, *supra* note 2, at 1769.

never a cash payment associated with these suits, and no reason to think that they lead to higher total attorneys' fee awards for plaintiffs' law firms, their most significant impact is likely a shifting of attorneys' fees among the plaintiff law firms that have brought these suits. The lawyers bringing the derivative claims seem to have a seat on the bus, but they are not driving it.

Prior to the lead plaintiff provisions enacted in the PSLRA, plaintiffs' lawyers filed multiple class action suits against the same company in the same federal court and, if the court did not name the first to file as lead plaintiff, it later worked out the individual roles in the litigation for each of the law firms involved under the umbrella of judicial supervision.¹³⁰ How different are law firm practices today? Given that this tagalong derivative litigation usually occurs before the same judge, and that most derivative suits are filed in the same jurisdiction as the prior class action suits, the possible abuses of multiple litigation and forum shopping seem muted.

As our theory predicts, this new form of derivative litigation arose because of changes in underlying legal rules that forced some existing plaintiffs' law firms to adjust their practices to maintain a seat at the settlement table. Other firms may have also entered the market when these new avenues for representative litigation opened up. Here, however, the resultant litigation agency costs seem muted, as the overall impact of the new cases appears largely to lead to a reallocation of attorneys' fees among plaintiffs' law firms.

2. *Deal Litigation.*—Mergers and other acquisitions frequently generate conflict between shareholders and managers. For example, management will regularly implement defensive tactics that block third-party offers at a price offering an attractive premium over the current market price. Alternatively, management may make a deal with a buyer that shareholders believe is too low, perhaps because the preferred bidder is the majority shareholder or a private equity group that is likely to retain current management. State corporation law, particularly in Delaware, has developed doctrines of fiduciary duty that provide the basis for such litigation.¹³¹ The multiplicity of suits that arise in this context will be governed by the law of the entity's state of incorporation, even if they are brought in different jurisdictions.¹³² This is the "internal affairs doctrine," a widely accepted feature in American jurisdictions that provides that internal

¹³⁰ See Weiss & Beckerman, *supra* note 9, at 2062. This is still common practice in mergers and acquisitions litigation, although as we noted above, cases are increasingly filed in different courts.

¹³¹ See *supra* note 19 and accompanying text.

¹³² See *Revlon, Inc. v. MacAndrews & Forbes Holdings, Inc.*, 506 A.2d 173, 182 (Del. 1986) (directors' duty in a takeover shifts to getting the best price for shareholders upon directors' decision to break up the company or put it up for sale); *Unocal Corp. v. Mesa Petroleum Co.*, 493 A.2d 946, 955 (Del. 1985) (defensive tactics in a takeover trigger intermediate judicial review where the board is required to show a threat and a proportional response).

governance rights of shareholders, directors, and officers should be determined by the law of the state where the entity is incorporated.¹³³

Deal suits are usually brought as class actions on behalf of the entire group of shareholders who have been harmed by the alleged misconduct (for example, seeking a higher dollar value than all the shareholders would have received had the directors not blocked an offer). Multiple suits are possible to the extent that different plaintiffs and different plaintiffs' law firms each step forward seeking to represent the group. Since Delaware is home to a large majority of America's largest corporations, its courts are a common venue for these suits. When multiple class actions arise in a single jurisdiction, as in Delaware, it is common to see a consolidation order overseen by a judge, which reflects a split of responsibilities worked out among the lawyers for the plaintiffs and presented as a proposed resolution to the judge.¹³⁴

Multiple suits challenging the same conduct in a deal may also be filed in more than one jurisdiction. Jurisdictional rules are such that in addition to the state of incorporation, it is also possible to bring the suit in courts of general jurisdiction of another state that has jurisdiction over the defendants.¹³⁵ In the corporate setting, this will be possible in the state where the company's headquarters is located. Alternatively, federal courts can hear these cases based on diversity jurisdiction.¹³⁶ These courts—the state court in the state of incorporation or a federal court hearing the case based on diversity—will apply the substantive law of the state of incorporation to all breach of fiduciary duty claims but provide an alternative forum that creates the possibility of multiple suits based on the same underlying facts.¹³⁷

Deal cases are filed in a particular state court as a result of a number of strategic considerations. Delaware, as the home to roughly 60% of America's public corporations, provides the setting where this choice has most often been visible.¹³⁸ Frequently, jurisdictional considerations dictate the choice to file in the Delaware Chancery Court (its law provides

¹³³ See *CTS Corp. v. Dynamics Corp. of Am.*, 481 U.S. 69, 89 (1987) (“No principle of corporation law and practice is more firmly established than a State’s authority to regulate domestic corporations . . .”).

¹³⁴ See *Hirt v. U.S. Timberlands Serv. Co.*, C.A. No. 19575, 2002 WL 1558342, at *2 (Del. Ch. Jul. 9, 2002) (noting the usual experience that plaintiffs and their counsel are able to negotiate an acceptable structure for the management of litigation “without involving the court in that process”).

¹³⁵ Each state determines the jurisdiction of its courts subject to constitutional limits of due process. The Supreme Court has held that as a general proposition a state cannot, by legislation, effectively divest other states’ courts of the power to hear cases over which they would otherwise have jurisdiction. See *Tenn. Coal, Iron & R.R. v. George*, 233 U.S. 354, 359–60 (1914).

¹³⁶ U.S. CONST. art. III, § 2.

¹³⁷ Other less common iterations of multiple suits arise from derivative suits, discussed in the following section, or a suit based on the proxy provisions of the federal securities law.

¹³⁸ Lucian Arye Bebchuk & Alma Cohen, *Firms’ Decisions Where to Incorporate*, 46 J.L. & ECON. 383, 391 tbl.2 (2003).

automatic jurisdiction over directors and officers of corporations chartered in the state¹³⁹) or in the state of the company's headquarters, where there is likely to be personal jurisdiction over the company and most of the individual defendants.¹⁴⁰

Some of the Delaware advantages described above have particular salience in the deal context. Delaware's ability to deliver a speedy resolution will be prized since the pending deal provides both parties reason to want to conclude the litigation while the money is still on the table. The expertise of the Delaware court may also be valued, since deals are often complex, and the parties stand to benefit by having a judge who has a background in the area.

Courts in a non-Delaware jurisdiction will be attractive to a plaintiffs' law firm that has reason to think it will be shut out from participating in the Delaware litigation or shunted to a less influential position with a smaller share of attorneys' fees. Delaware courts have moved toward a lead plaintiff approach similar to that implemented under the PSLRA. As a result, attorneys who do not have the client with the largest financial interest, or some other expertise that will cause them to be picked by the chancery court, will see the virtue of filing in a second jurisdiction. This may enable the firm to get a seat at the table that it would not have been able to obtain in Delaware when the time comes to settle the cases. Alternatively, the second attorney may even be able to get control of the case by persuading the court in the headquarters jurisdiction to decide the case and then seek *res judicata* preclusion of the other case under *Matsushita*.¹⁴¹ The second attorney may be aided in this strategy by the support of the attorneys for the defendant who see the second jurisdiction and the second plaintiffs' attorney as more amenable to settling the case on terms that are favorable to the corporation. In such a setting, the defendants may be able to launch a reverse auction among plaintiffs' firms and drive down the costs for settling the case.¹⁴²

Courts in the non-Delaware jurisdiction may also be attractive for other reasons. The sometimes-expressed hostility to liberal attorneys' fees in Delaware has already been mentioned. In addition, Delaware traditionally has not permitted discovery prior to a motion to dismiss in derivative suits,¹⁴³ a practice that predates the federal law's adoption of a similar rule for class actions in the PSLRA and which makes it more difficult for the

¹³⁹ DEL. CODE ANN. tit. 10, § 3114(a) (1999 & Supp. 2010).

¹⁴⁰ See *supra* note 46 and accompanying text. Federal courts may also hear deal litigation under federal question jurisdiction if the complaint also raises claims for false and misleading proxy disclosures under § 14 of the 1934 Exchange Act. Interview with plaintiffs' lawyer (Jan. 31, 2012) (on file with authors).

¹⁴¹ *Matsushita Elec. Indus. Co. v. Epstein*, 516 U.S. 367 (1996); see *supra* note 62 and accompanying text.

¹⁴² See *infra* note 257 and accompanying text.

¹⁴³ *Delaware Balancing*, *supra* note 4, at 1379.

plaintiff's case to get past that initial hurdle. Procedural rules in other states are not always as severe and, under prevailing doctrine, those states can apply their own procedural rules even when they must apply the substantive rules of the state of incorporation.¹⁴⁴

Our prior study of Delaware litigation over a two-year period illustrates many of these factors in the deal litigation context. We found that litigation against publicly held companies overwhelmingly arose out of deals and was in the form of class actions as opposed to derivative suits.¹⁴⁵ Generally, multiple suits are filed very quickly after the announcement of a deal, by law firms who are repeat players in such litigation.¹⁴⁶ Data from the suits that produced settlements indicated that suits in which managers had a conflict of interest in the proposed deal were the most likely to produce cash settlements,¹⁴⁷ and that these deal suits did not indicate the same degree of litigation agency costs as suggested for earlier representative suits.¹⁴⁸ Subsequent expansion of this data set to include all litigation arising out of deals in this two-year period found that 12% of deals had litigation; litigation decreased the likelihood of a deal closing, but also increased return on the deals that closed, so that overall it was associated with an increased return for the deals where there was litigation.¹⁴⁹

Recent empirical studies provide information on deals in a broader time period and focus on particular aspects of these deals. Armour, Black, and Cheffins, for example, developed a data set of the top twenty-five M&A deals each year for a fifteen-year period beginning in the mid-1990s. Delaware firms, which made up two-thirds of their sample, were sued in 47% of the deals, with a surge between 2005 and 2009.¹⁵⁰ During this more recent period, the growth in large deal litigation was in suits filed in states other than Delaware, so that all litigation was outside Delaware in almost half of the cases filed.¹⁵¹ Litigation in federal courts in this data set was considerably less frequent.¹⁵²

Professors Armour, Black, and Cheffins have a second data set of all leveraged buyout transactions over a fifteen-year period that produced similar results.¹⁵³ Delaware firms made up 63% of the sample, and again,

¹⁴⁴ RESTATEMENT (SECOND) OF CONFLICT OF LAWS § 302 cmt. d (1971) (“[A] court under traditional and prevailing practice will apply its own state’s rules involving process, pleadings, joinder of parties, and the administration of the trial . . .”).

¹⁴⁵ *New Look*, *supra* note 5, at 137.

¹⁴⁶ *Id.* at 138.

¹⁴⁷ *Id.* at 199 tbl.17.

¹⁴⁸ *Id.* at 192–98 (suggesting a lower percentage of recovery for attorneys and a greater percentage of cases producing some financial benefit for shareholders).

¹⁴⁹ *Litigation in Mergers*, *supra* note 5, at 2, 20.

¹⁵⁰ *Delaware Balancing*, *supra* note 4, at 1356–57 & fig.3.

¹⁵¹ *Id.* at 1356.

¹⁵² *Id.* at 1358 fig.4.

¹⁵³ *Id.* at 1360 & fig.6.

47% of the Delaware firm deals involved litigation.¹⁵⁴ The trend for litigation to occur in Delaware—73% in the 1997–2001 part of the study—declined in the 2005–2009 period.¹⁵⁵ Again, suits in federal courts made up a smaller portion of the study.¹⁵⁶

Studies by two other scholars confirm a similar split in where litigation occurs. Professor Jennifer Johnson's 2010 sample of class actions found that 45% occur in states other than Delaware, 40% in Delaware, and 18% in federal court.¹⁵⁷ Professor Brian Quinn's study of deals done in 2009–2010 found that 40% of litigation is outside of Delaware and the incidence of deals leading to suits is even higher.¹⁵⁸ None of these studies present data on the outcome of the litigation.

Two other studies provide information about the outcome of litigation. Robert Daines and Olga Koumrian's study for Cornerstone Research, which collected data through early 2012, found that Delaware's share of M&A litigation increased steadily after 2008.¹⁵⁹ Their study of challenges to 2010 and 2011 M&A deals found that 67% settled and that 83% of the settlements were for additional disclosure only.¹⁶⁰ Professors Cain and Davidoff's sample of litigation arising from deals between 2005 and 2010 found a settlement number in the same range with a smaller number of disclosure-only settlements.¹⁶¹ Both studies tracked attorneys' fees, the Cain and Davidoff study reporting data for a much larger percentage of settlements but with mean and median figures in the same range.¹⁶²

What are we to make of these empirical studies? Deal litigation appears to be a large and distinct category of representative litigation. These suits are usually brought as class actions under the corporation law of the entity's state of incorporation. There have long been multiple suits in the same jurisdiction arising out of the same deal as different plaintiffs and their law firms seek to represent the class. Over time, more of these suits

¹⁵⁴ *Id.* at 1359.

¹⁵⁵ *Id.* at 1360.

¹⁵⁶ *Id.* at 1360–61 & fig.7.

¹⁵⁷ Johnson, *supra* note 3, at 377 fig.11 (reporting 265 filings against 193 Delaware companies of which 103 were in Delaware, 115 were in another state, and 47 were in federal court).

¹⁵⁸ Quinn, *supra* note 4, at 147.

¹⁵⁹ ROBERT M. DAINES & OLGA KOUMRIAN, CORNERSTONE RESEARCH, RECENT DEVELOPMENTS IN SHAREHOLDER LITIGATION INVOLVING MERGERS AND ACQUISITIONS: MARCH 2012 UPDATE 6 tbl.5 (2012), available at http://www.cornerstone.com/files/Publication/2af469a2-f24a-4435-96c0-a36d24a541ae/Presentation/PublicationAttachment/876cdfd2-d105-408e-ae0-a37fe880c07a/Cornerstone_Research_Shareholder_MandA_Litigation_03_2012.pdf (reporting increase from a 34% share in 2007 to a 45% share in 2011 and 2012).

¹⁶⁰ *Id.* at 9, 11 (results from a sample of 202 settlements related to 2010 and 2011 litigation).

¹⁶¹ Cain & Davidoff, *supra* note 36, at 33 tbl.2 (reporting settlements in 69.8% of 447 litigation outcomes over the 2005–2010 period while only making up 52% of the litigation sample).

¹⁶² *Id.* at 34 tbl.2 (reporting mean attorneys' fees of \$1.27 million and median of \$595,000 for settlements of litigation of 2010 deals). Daines & Koumrian show a median and mean in the same range with fee data from 88 of the 202 deals with litigation. DAINES & KOUMRIAN, *supra* note 159, at 12.

have moved beyond Delaware to be litigated elsewhere, most often in the courts of the entity's headquarters state, and often suits are filed in both venues.

This change does not reflect differences in substantive laws, as most of these suits seek to apply Delaware law. Rather, filings in non-Delaware jurisdictions are driven by plaintiffs' law firms' interests as firms seek to gain shares of any potential attorneys' fees awards. They may also reflect a hostility to attorneys' fees awards, perceived in some opinions of the Delaware Chancery Court,¹⁶³ although there is more recent judicial language suggesting a somewhat different approach to attorneys' fees.¹⁶⁴ The addition to the plaintiffs' bar of new small firms may be driving a broader geographical search for lawsuits.¹⁶⁵ Smaller, less well-established firms are less likely to win in Delaware's lead plaintiff contest,¹⁶⁶ forcing them to file in other jurisdictions to get a share of any attorneys' fee awards. Another contributing factor may be that one of the more visible plaintiffs' firms, Milberg Weiss, split into east and west coast branches and later suffered losses when several partners went to jail related to behavior with clients in class actions.¹⁶⁷ This led to more suits being filed outside of Delaware by the spin-off firm of Lerach Coughlin.¹⁶⁸ As a more diverse plaintiffs' bar has grown up, these lawyers may be more comfortable outside of Delaware or at least may like having an additional place to bring suit. We consider the possibility for reform in Part II.

Shifts in federal substantive and procedural rules led plaintiffs' law firms to shift representative litigation into mergers and acquisitions class action litigation. As more firms crowded into the field, they took advantage of the possibility of filing multiple suits in a single state court, usually Delaware's Chancery Court. Plaintiffs' lawyers' perceptions that this court had become less hospitable to their cases (combined with legal innovations in Delaware procedures) in turn led those firms to move further afield to file

¹⁶³ See, e.g., *In re Revlon, Inc. S'holders Litig.*, 990 A.2d 940, 959 (Del. Ch. 2010) ("There are sound policy reasons for this Court to police against shirking by representative counsel."); *In re Cox Commc'ns, Inc. S'holders Litig.*, 879 A.2d 604, 640-42 (Del. Ch. 2005) (lowering the award of attorneys' fees in a successful shareholder litigation to something that can more "reasonably be justified").

¹⁶⁴ See Cain & Davidoff, *supra* note 36, at 2 (reporting Delaware Chancellor's promotion of Delaware courts "as a friendly haven for plaintiffs' attorneys to bring meritorious class action[s]").

¹⁶⁵ Telephone Interview with plaintiffs' lawyers (July 25, 2011).

¹⁶⁶ See *infra* Part II.C.4.

¹⁶⁷ Heidi Moore, *Double Trouble*, THE DEAL (May 10, 2004) (announcing the breakup of the Milberg Weiss firm) (available at LexisNexis); see generally Lisa L. Casey, *Class Action Criminality*, 34 J. CORP. L. 153, 154 n.1, 160-61 (2008) (detailing the firm's split, the criminal prosecution of four of the firm's partners, and the firm's \$75 million settlement with the government).

¹⁶⁸ "When Lerach Coughlin, the predecessor of Robbins Geller, split off from Milberg, they said, as their business plan, we are going to sue elsewhere. We're not going to sue in Delaware." Transcript of Plaintiffs' Motion for a Preliminary Injunction and the Court's Ruling at 19, *In re Compellent Techs., Inc. S'holders Litig.*, C.A. No. 6084-VCL (Del. Ch. Jan. 13, 2011).

mergers and acquisitions representative suits in other states' courts and federal courts. This form of forum shopping resulted, which may have increased litigation agency costs.

3. *Traditional Derivative Suits.*—Traditional derivative litigation is the third important type of representative litigation that generates multiple suits. These cases raise state law breach of fiduciary duty claims by directors and officers. Typically, these claims include breach of the duties of loyalty—including good faith—and care, as well as other state law issues. Derivative suits are the traditional form of representative litigation and are used to attack directors or officers who are engaging in conflict-of-interest transactions with the corporation or are taking a corporate opportunity belonging to the corporation. A recent prominent example is the options backdating scandal, in which a number of large corporations were found to have provided their executives with options to buy stock on dates and terms that were backdated so that the option appeared to have been granted before a subsequent (favorable) event had occurred.¹⁶⁹ In reality, since the option price was not set until after a significant financial event had occurred, backdating increased the likely value of the option, since it was closer to a sure bet.¹⁷⁰ Research by professors and news services led to government regulatory investigations that revealed wide-ranging misbehavior and resulted in a series of derivative suits to recover benefits that insiders unjustly obtained from the corporation.¹⁷¹

As a substantive matter, these traditional derivative cases will be determined by the law of the state of incorporation. As with our prior category, deal litigation, the forum for litigation could be the state courts of the state of incorporation (as above, often Delaware), a court in another state where the company is headquartered, or any federal court if appropriate jurisdiction can be established.

In contrast to deal cases, there is no pending transaction overshadowing the litigation that makes time so important and litigation more rapid. Moreover, litigation in these derivative cases is likely to be more complex than in deal cases. Different procedural requirements, such as the requirement for demand on the directors to bring suit, means that there can be more pretrial motions, which could deter certain types of plaintiffs' law firms. These two factors, the less pressing impact of time and

¹⁶⁹ See *Delaware Balancing*, *supra* note 4, at 1362–63 (discussing data relating to option backdating cases).

¹⁷⁰ M.P. Narayanan et al., *The Economic Impact of Backdating of Executive Stock Options*, 105 MICH. L. REV. 1597, 1602 (2007) (providing an example of a typical backdating transaction and how it permits directors and executives to receive stock that is “in-the-money immediately”).

¹⁷¹ See Charles Forelle & James Bandler, *The Perfect Payday*, WALL ST. J., Mar. 18, 2006, at A1; see also Ryan v. Gifford, 918 A.2d 341, 360 n.60 (Del. Ch. 2007) (detailing scholarly research on the backdating controversy); Shannon German, *What They Don't Know Can Hurt Them: Corporate Officers' Duty of Candor to Directors*, 34 DEL. J. CORP. L. 221, 235 (2009) (explaining how a *Wall Street Journal* piece led to the investigation of 130 companies for backdating).

the greater likelihood of more intense pretrial litigation, may also dampen the impact of reverse auctions by reducing the range of plaintiffs' law firms likely to bring litigation.¹⁷² These litigation factors will interact with law firm size and resources to affect what type of law firm files these cases.¹⁷³

A plaintiff law firm in these suits may choose a forum to gain a more attractive platform for prosecuting and settling the litigation, as discussed above, or because of procedural differences in how different jurisdictions will handle the derivative suits. For example, there may be differences in discovery rules among jurisdictions.¹⁷⁴ Delaware has long followed a pattern of declining to permit discovery in derivative cases prior to a motion to dismiss.¹⁷⁵ This rule mirrors the PSLRA, but actually predates that federal rule. If other states do not have such a rule, they may present a more attractive venue.¹⁷⁶ States may also differ on how they approach demand requirements under derivative suits. Delaware, for example, requires demand unless it is excused,¹⁷⁷ so that much of the litigation is over whether the requirements for demand excusal were met. Other states require universal demand.¹⁷⁸ Some states also require plaintiffs to post bond for the likely expenses incurred by the defendants in responding to the lawsuit.¹⁷⁹

Once an initial suit has been filed, either in Delaware or the state of the corporation's headquarters, there are sometimes suits filed in other jurisdictions. If the initial plaintiff made its forum selection based on procedural advantages, one wonders what motivates the second plaintiff to file in a procedurally less favorable jurisdiction. We think that there are at least two factors that are important here: first, the Delaware lead plaintiff provision may shut out smaller, newer plaintiffs' law firms from that state, and second, the potential for getting a part of a global settlement, or conducting a reverse auction, may support filing elsewhere.

Armour, Black, and Cheffins have developed the most complete data set of backdating cases. They find 165 firms with either federal or state

¹⁷² See *supra* Part I.A.4.a (discussing plaintiffs' firms).

¹⁷³ Firms that lack the resources to litigate these intensive matters may choose not to file them. However, it is also possible that weaker firms may simply file weaker cases and seek to settle them cheaply.

¹⁷⁴ See *Delaware Balancing*, *supra* note 4, at 1379 (discussing Delaware as part of a minority of states that stay discovery in a derivative action until a motion to dismiss has been heard).

¹⁷⁵ See, e.g., *Rales v. Blasband*, 634 A.2d 927, 934 & n.10 (Del. 1993) (addressing alternative means for a plaintiff to plead with particularity).

¹⁷⁶ See *Delaware Balancing*, *supra* note 4, at 1379 (stating that Delaware is one of a minority of states that stay discovery in a derivative suit).

¹⁷⁷ *Aronson v. Lewis*, 473 A.2d 805, 815 (Del. 1984).

¹⁷⁸ See MODEL BUS. CORP. ACT § 7.42 (2011) (requiring universal demand on directors prior to bringing a derivative suit). The MBCA lists states with similar statutes requiring universal demand. See 2 MODEL BUS. CORP. ACT ANN. § 7.40, at 7-294 to -95 (4th ed. 2008 & Supp. 2011).

¹⁷⁹ See, e.g., N.Y. BUS. CORP. LAW § 627 (McKinney 2003 & Supp. 2012).

lawsuits relating to backdating, with Delaware-incorporated firms accounting for 77% of the defendant companies.¹⁸⁰

Litigation filing patterns for this set of cases differ from those discussed above. For backdating cases, about half of the suits were brought in federal court, 40% in the courts of states other than Delaware, and only 11% in Delaware.¹⁸¹ According to Erickson, these suits are not likely to be associated with parallel securities fraud class actions, although they are usually associated with SEC investigations.¹⁸²

Both Erickson and Armour, Black, and Cheffins report that backdating cases frequently produce cash awards in settlements. Erickson finds cash settlements in 17 of her 40 public company backdating cases filed in federal courts, as compared to 2 of 101 other, non-backdating-related derivative suits.¹⁸³ Armour, Black, and Cheffins report a somewhat smaller percentage of backdating suits producing cash recoveries (52 of 165) in their backdating sample.¹⁸⁴

These backdating suits look more like the ones in our earlier study of derivative suits filed in Delaware, where we found derivative suits often raised conflicts of interest related to a particular transaction.¹⁸⁵ There we also found some derivative suits, brought on *Caremark* grounds,¹⁸⁶ alleging breaches of directors' duty of care where the board had not uncovered problems that led to a regulatory investigation and a large fine. Such claims could be brought in the Delaware Chancery Court, but the *Caremark* standard, while amorphous, has not been interpreted by the Delaware judges to impose much in the way of personal liability on directors or officers.¹⁸⁷ More often, these cases seem to be brought in state courts in the headquarters state of the company, although the more recent data sets do not provide data on this question.¹⁸⁸ In these cases, there appear to be relatively weak claims that can proceed in tandem with negotiations with

¹⁸⁰ *Delaware Balancing*, *supra* note 4, at 1363.

¹⁸¹ *Id.*

¹⁸² Erickson, *supra* note 2, at 1759, 1810 & n.228 (stating that stock option suits were filed exclusively against large public companies).

¹⁸³ *Id.* at 1798.

¹⁸⁴ *Delaware Balancing*, *supra* note 4, at 1390.

¹⁸⁵ *Derivative Lawsuits*, *supra* note 5, at 1786 (“[T]he bulk of all public company derivative suits challenge conflict of interest transactions . . .”).

¹⁸⁶ *In re Caremark Int'l Inc. Derivative Litig.*, 698 A.2d 959 (Del. Ch. 1996).

¹⁸⁷ Some federal courts have been more willing to find fiduciary violations under state law in a care setting, as for example, in *In re Abbott Labs. Derivative S'holders Litig.*, 325 F.3d 795, 803–09 (7th Cir. 2003) (using Delaware precedents to interpret Illinois corporate law and finding complaint sufficiently pled director action outside the business judgment rule). As a result, we would expect to see more such cases filed in federal court in the same circuit where plaintiffs could take advantage of the favorable interpretation of Delaware law.

¹⁸⁸ Most state courts do not have electronic filing systems, which makes research about state court derivative actions outside of Delaware very difficult. *See supra* note 115.

the Department of Justice or states' attorneys general, and which often result in corporate governance settlements.¹⁸⁹

These traditional derivative suits are probably the most stable set of cases of all of the representative litigation groups. There has been little change in the underlying set of legal and procedural rules for derivative litigation in the past twenty years, although pressure on other areas of representative litigation seems to have resulted in new firms moving into the field. While the increased number of smaller plaintiffs' law firms could lead to more multijurisdictional derivative litigation, we do not presently have good data about the size or existence of this potential problem. As a result, we cannot make strong statements about litigation agency cost issues at this point.

II. DEFINING THE MULTIJURISDICTIONAL PROBLEM CONFRONTING REPRESENTATIVE SHAREHOLDER LITIGATION AND HOW IT SHOULD BE ADDRESSED

Shareholder litigation, with its multiple sources of legal rules and its multiple agents desiring to speak for the group, has long generated multiple lawsuits arising from the same underlying activity. Each participant in the process plays a role in this: the plaintiffs' law firms have incentives to seek out different courts for suits arising out of the same transactions, the defendants have little reason to object to them doing so, and the courts may indirectly encourage this practice by competing to get these cases. Such suits have always presented a tradeoff between the desirable check of possible misuse of the broad powers corporate law provides managers and the costs of litigation agents diverting the process for their own benefit. Recent articles and press coverage of deal litigation have focused on the increase in the number of deals attracting litigation as the latest presentation of this conflict and have proposed a variety of reforms.¹⁹⁰

In this Part, we use the theory of shareholder litigation and description of the various litigation patterns developed in Part I to address the particular context of multijurisdictional shareholder litigation. We begin in section A with some initial comments about the nature of the problem as revealed by the studies described in the previous Part. We see the primary focus not as the increase in the number of deals attracting litigation, but rather as an

¹⁸⁹ Erickson, *supra* note 2, at 1804.

¹⁹⁰ See, e.g., *Delaware Cases*, *supra* note 4 (addressing an increase in litigation outside Delaware); Kazanoff, *supra* note 76, at 42; Edward B. Micheletti & Jenness E. Parker, *Multijurisdictional Litigation: Who Caused This Problem, and Can It Be Fixed?*, 37 DEL. J. CORP. L. 1, 4 (2012) (noting that deal litigation has become "a routine facet" of a deal); Dionne Searcey & Ashby Jones, *First the Merger; Then the Lawsuit*, WALL ST. J., Jan. 10, 2011, at C1 (citing an "ever-increasing number of lawsuits" that threaten to "increase the cost of the transactions"); Jessica Silver-Greenberg, *Why Merger Lawsuits Don't Pay*, WALL ST. J., Aug. 27, 2011, at B9 (citing a record number of deals lawsuits but noting that "legal experts warn that the chances [litigants] will succeed in stopping a deal or receiving a significant payday are minimal").

increase in the amount of multijurisdiction litigation. This framing of the problem highlights the need to include analysis of traditional issues from the larger field of procedural law, such as forum selection and forum shopping, in this analysis of shareholder litigation. Our discussion in section B develops how the particular characteristics of shareholder litigation shift and narrow the impact of these procedural issues as compared to litigation generally, shifting the focus more to attorneys rather than plaintiffs. In multijurisdictional deal litigation, the primary economic motivation is to provide an entry to a second set of attorneys seeking to get a piece of a pool of attorneys' fees in deals expected to generate attorneys' fees; it is not to generate strike suits. Section C provides an exploration of different solutions currently being debated to change this multijurisdictional shareholder litigation pattern—judicial, legislative, and through private ordering by the various corporate constituencies. Procedural concerns about forum selection and forum shopping play out somewhat differently in the shareholder litigation context than in litigation generally. Our theory suggests a solution that focuses on judicial cooperation as the most effective response among the multiple solutions being debated.

A. What the Pattern of Shareholder Litigation Tells Us About the Problem

Shareholder litigation has long raised the possibility of strike suits. Some litigation agency costs can be accepted as a necessary tradeoff between having an effective litigation vehicle to permit courts to monitor possibly injurious management behavior and balancing additional constraints to check disincentives that can arise for plaintiffs in shareholder suits. We begin with three takeaways from our theory (discussed in the prior Part) and the empirical data generated about shareholder litigation, which narrows and reshapes both the problem and the preferred solutions.

First, the increase in the percentage of deals attracting litigation has gotten the most attention from the press,¹⁹¹ but the best data available does not indicate any pattern of increase in the total number of deals that attract litigation.¹⁹² In a recent working paper, Professors Cain and Davidoff report hand-collected data showing that the total number of deals attracting litigation changed very little from 2006 to 2011.¹⁹³ However, in the post-financial crisis period, the number of deals dropped substantially.¹⁹⁴ The combination of these two factors means that the percentage of deals

¹⁹¹ See *supra* note 190.

¹⁹² There is no good data source on the level of multijurisdictional derivative litigation. See *supra* note 115.

¹⁹³ Cain & Davidoff, *supra* note 36, at 31 tbl.1 (showing that in 2006 and 2007, 97 deals per year attracted litigation, whereas 2008 (50 deals) and 2009 (60 deals) showed declines in the number of deals attracting suits, and 2010 had 101 deals with litigation); see also DAINES & KOURMIRAN, *supra* note 159, at 2 tbl.1 (showing through 2011 that the deals litigated have been right at Cain & Davidoff's average for the previous six years).

¹⁹⁴ Cain & Davidoff, *supra* note 36, at 31 tbl.1.

attracting litigation increased markedly in 2009 and 2010.¹⁹⁵ This increased percentage of cases attracting litigation could be a problem if additional sums, such as extra attorneys' fees, were paid to settle cases in which there was no real benefit to shareholders, or if it resulted in lower quality cases being brought.¹⁹⁶ The rise in the number of settlements that provide only additional disclosure (and attorneys' fees) could be indicia of this.¹⁹⁷ However, lawsuit quality is difficult to assess and could be the result of a large number of factors for which we do not yet have empirical results.¹⁹⁸ Overall, Cain and Davidoff report a mean amount of attorneys' fees paid in settled cases in the last year of their study that is below the six-year average and a median that is slightly above the six-year average.¹⁹⁹

Cain and Davidoff report that the mean number of suits per case doubled from 2005 to 2009 and 2010, and the percentage of deals with multijurisdictional litigation increased substantially during those same years.²⁰⁰ Taken together, this finding and the previous ones indicate that the problem we are addressing is an increase in the amount of multijurisdictional litigation and not an increase in the number of deals attracting litigation.

¹⁹⁵ *Id.* (reporting a strong increase in the percentage of deals from 2005 (38.7%) to 2011 (84.2%)). Other papers report a similar increase in the percentage of deals attracting litigation without addressing the number of suits. *See, e.g.,* Quinn, *supra* note 4, at 148 tbl.1 & 2 (showing that 82% of public mergers were accompanied by some litigation in 2009 and 2010).

¹⁹⁶ Cain & Davidoff report outcome data for their sample, but it is not broken out by year with one exception. They do find an increase in the number of disclosure-based settlements over their sample period. *See* Cain & Davidoff, *supra* note 36, at 34 tbl.2.

¹⁹⁷ Cain & Davidoff's data from 2005 to 2010 on the percentage of settlements that do not involve disclosure claims only show a marked decline in this percentage after 2006. *Id.* Daines & Koumrian show a similar percentage into 2011. DAINES & KOUMRIAN, *supra* note 159, at 12. Both show a much higher percentage of settlements and settlements with only additional disclosure than we found in our study of litigated merger deals in 1999 and 2000. *See New Look, supra* note 5, at 181 tbl.8.

¹⁹⁸ If disclosure-only settlements are weaker settlements, which would be consistent with the lower attorneys' fees awards reported in these suits, this could indicate a decline in the quality of settlements over the past few years. However, any such change could be a result of a large number of factors, such as a change in deal quality or a shift in judicial attitudes toward disclosure-only settlements. No causal link to multijurisdictional litigation has been established by any empirical studies. Furthermore, if lawsuit quality is dropping, the courts have a number of techniques that they can employ to directly address that problem, such as denying motions for expedited discovery, denying attorneys' fees, or outright dismissal of the action. *See, e.g.,* Transcript of Teleconference on Plaintiff's Motion to Expedite and the Court's Ruling at 11–14, *Stourbridge Invs. LLC v. Bersoff, C.A. No. 7300-VCL (Del. Ch. Mar. 13, 2012)* (denying expedited discovery in a disclosure-only settlement case “[g]iven the nature of the complaint and its significant weaknesses . . .”). Given their prominence, if the Delaware courts took the lead in using such techniques against poor cases, other courts would be likely to follow suit.

¹⁹⁹ Cain & Davidoff, *supra* note 36, at 34 tbl.2 (showing that mean attorneys' fees in 2005 was \$1.77 million versus in 2010 when the mean value was \$1.27 million; the median value in 2010 was \$595,000 against a six-year average of about \$558,000); *see also* DAINES & KOUMRIAN, *supra* note 159, at 12 & fig.5 (showing similar fee data for 2010 and 2011—\$1.2 million for a mean and between \$500,000 and \$600,000 for a median attorneys' fee award). Data concerning defendants' attorneys' fees is not disclosed in settlements and remains private information so we cannot tell what, if any, impact the increased percentage of deals being litigated has had on them.

²⁰⁰ Cain & Davidoff, *supra* note 36, at 31.

Second, these multijurisdictional cases all revolve around which court will be applying the law of the state of incorporation and not around the choice of law to be applied. As a result, these cases raise a narrower set of issues than forum selection claims more generally. To be sure, different courts in different jurisdictions may have slightly different ways of interpreting the underlying legal principles of the state of incorporation, but whether it is a state court in the defendant company's headquarters state, a federal court sitting in a diversity case (or deciding a pendent state law claim), or the trial court in the state of incorporation, there is no dispute that the internal affairs doctrine makes the law of the state of incorporation the appropriate source for legal rules.²⁰¹ At the same time, these cases raise concerns more specific to corporate litigation, such as whether the state of incorporation's interest in determining its law should have a greater role than in other forum selection contexts, and who in the corporation should be able to make forum selection choices. We discuss these two points below.

Third, the lack of a method to consolidate all class action and derivative cases arising out of the same set of facts also shapes the footprint for possible solutions. There are federal procedural rules to permit federal securities fraud class actions to be assembled before one judge,²⁰² and when multiple cases are filed within the courts of one state, consolidation orders are widely used so that all discovery efforts will be processed efficiently and motions can be decided with respect to the entire matter.²⁰³ However, the rise in litigation that we trace in Part I mostly results from multiple cases filed in different states, or in federal courts as well as state courts, where the judicial system has no internal mechanism to ensure that all cases wind up in front of one judge.

As we discuss more fully below, each of these points narrows both the problem and the effectiveness of several of the proposed solutions. In the remainder of this section, we show that this litigation does not raise the traditional issues related to forum shopping but rather raises a new issue: fee distribution litigation. That is, these cases are usually brought to give the plaintiffs' law firms filing them a claim to a place at the settlement table and not because they offer the plaintiffs the traditional advantages of forum shopping, such as a better choice of law or a judge perceived to be friendly on the substantive law. We then test various potential judicial solutions against this reality, finding that there are real limits to some of the alternatives, leaving what some will find, perhaps, a surprising favorite.

²⁰¹ See *supra* note 133 and accompanying text.

²⁰² 28 U.S.C. § 1407 (2006). The lead plaintiff and MDL provisions actually speak only to pretrial matters, but that effectively covers all matters because few of these cases ever go to trial. See Cox et al., *supra* note 77, at 428.

²⁰³ See *New Look*, *supra* note 5, at 168.

B. Multijurisdictional Representative Shareholder Litigation: Is It Motivated by Traditional Forum Shopping Concerns?

The American legal system generally creates more than one legally acceptable forum that can hear a case and gives the plaintiff the initial choice of where to file. This protects the plaintiff's ability to reach a defendant in a court with jurisdiction, provides an option that can reduce costs, and limits the possible discrimination of local courts against parties from other jurisdictions. It also raises a countervailing inquiry: is the plaintiff's choice of a particular court merely forum selection, which is necessary in all litigation, or is it forum shopping, which is frequently condemned by courts and commentators?²⁰⁴ No clear point exists at which forum selection becomes forum shopping.

To draw a meaningful line between the two, we need to define forum shopping. In its broadest form, "[f]orum shopping is a plaintiff's decision to file a lawsuit in one court rather than another potentially available court."²⁰⁵ However, this definition is too broad because it would render all forum selection decisions forum shopping. More generally, forum shopping requires that more than one court be available to resolve the plaintiff's claim and that the plaintiff "may be more likely to win . . . in some legal systems than in others," so as to create an incentive to forum shop.²⁰⁶ In such a setting we would expect a plaintiff to choose the court with the highest expected value for her claims (value of settlement minus costs), which depends on the judge being willing to hear the case (implicating issues related to personal jurisdiction, subject matter jurisdiction, and proper venue) and on which jurisdiction's laws will apply (choice of law decisions).²⁰⁷ Forum shopping could be defined even more broadly to include other types of differences between jurisdictions that may influence substantive results, including the reputation of the judge likely to hear the case, the likelihood of a favorable jury pool, prior judicial decisions or jury verdicts in similar matters, and the convenience of the particular forum.²⁰⁸

Forum shopping is not limited to plaintiffs, either—defendants frequently take actions to move cases to forums that they perceive as more

²⁰⁴ See ROBERT C. CASAD, JURISDICTION AND FORUM SELECTION § 1:01 (2d ed. 1999).

²⁰⁵ Christopher A. Whytock, *The Evolving Forum Shopping System*, 96 CORNELL L. REV. 481, 485 (2011). Other authors have taken a wider perspective on what constitutes forum shopping. See Debra Lyn Bassett, *The Forum Game*, 84 N.C. L. REV. 333, 345–46 (2006) (describing five basic types of forum shopping as: (1) choosing between federal and state courts, (2) choices among different state courts, (3) selecting among different substantive legal rules, (4) choosing among different procedural rules, and (5) choices involving personal or subjective matters).

²⁰⁶ Whytock, *supra* note 205, at 486.

²⁰⁷ Choice of law differences can be because of differences in state law, substantive legal rules, or choice of law rules.

²⁰⁸ See Bassett, *supra* note 205, at 350. While this definition is more accurate in capturing the concept of strategic litigation, it is more far-reaching than what most courts and commentators have in mind when they discuss forum shopping.

favorable.²⁰⁹ Defendants have a broad set of standard forum shopping techniques, such as removing cases from state to federal court, filing motions asking judges to stay one action in favor of another action, making challenges to a court's ability to exercise personal jurisdiction or subject matter jurisdiction, using a forum non conveniens motion to claim that a particular venue is improper, and, in some cases, filing declaratory judgment actions to fix a particular venue for the litigation before a plaintiff can file a complaint. Forum selection clauses in contracts or corporate governing documents (most often inserted by defendants) are another device for forum shopping, as they ensure the defendant's choice of the applicable court, legal rules, and choice of law rules, no matter how inconvenient or potentially dispositive of the plaintiff's case.²¹⁰

1. Forum Choice as Part of Core Procedural Rules.—One of our favorite Civil Procedure teachers tells her 1L students each year that litigation is like a chess match: each side has certain moves that it is allowed to make, and the other side responds as it deems appropriate based on the moves permitted under the rules. In chess, white moves first and can make certain moves; in most litigation, the plaintiff moves first and has certain permissible forums. Just as in chess, the plaintiff's choice of forum should be respected so long as it chooses a fair forum within the set of possible forums.²¹¹ The fact that the rules of civil procedure allow the plaintiff to choose, among the multiple permissible forums, where to file a suit is one of the strongest arguments in favor of forum shopping.²¹²

The fact that plaintiffs may choose one forum over another does not mean that they are cheating in the litigation "chess game" so long as they are playing within the procedural and substantive rules. Forum choice is only one of the rules of the chess match, and, while some aspects of the rules may favor plaintiffs, others favor defendants. For example, plaintiffs must pay the costs associated with researching and filing a case, spend the time, and overcome significant informational barriers to uncover proof of alleged wrongs committed by the defendants—information that is generally in the defendants' sole possession. In the corporate litigation context, defendants have many other advantages, such as the high procedural barriers for pleading cases without access to discovery.²¹³ Businesses have already been given a significant forum shopping opportunity, as entrepreneurs and managers make the initial choice of where to

²⁰⁹ CASAD, *supra* note 204, §§ 1.06–1.08.

²¹⁰ See Linda S. Mullenix, *Another Easy Case, Some More Bad Law: Carnival Cruise Lines and Contractual Personal Jurisdiction*, 27 TEX. INT'L L.J. 323, 360–61 (1992).

²¹¹ See Earl M. Maltz, *Choice of Forum and Choice of Law in the Federal Courts: A Reconsideration of Erie Principles*, 79 KY. L.J. 231, 249 (1990–91).

²¹² See Antony L. Ryan, *Principles of Forum Selection*, 103 W. VA. L. REV. 167, 202 (2000).

²¹³ See *supra* note 10 and accompanying text.

incorporate.²¹⁴ In many cases, as noted above, they may also choose forum selection clauses that funnel all disputes into one court. In short, plaintiffs' ability to select a forum is just a small aspect of a procedural structure that, as a whole, does not favor plaintiffs over defendants.

Moreover, the plaintiff's attorney has a legal obligation to choose the best forum for her client.²¹⁵ Ethical rules require a lawyer to zealously pursue the interests of her client within the bounds of the law. This includes selecting the most favorable forum for her client when it furthers the client's interests, so long as the lawyer is not trying to delay, harass, or maliciously injure the defendant.²¹⁶

2. *Common Arguments Against Forum Shopping.*—Arguments against forum shopping are long standing and can apply in the corporate context. Critics of forum shopping frequently argue that the U.S. Supreme Court has condemned forum shopping, citing the classic 1938 case of *Erie Railroad Co. v. Tompkins*.²¹⁷ There the Court took aim at one form of forum shopping: plaintiffs' efforts to choose between federal and state courts based on federal judges using federal common law to interpret state substantive law.²¹⁸ Although it condemned such state–federal forum shopping, it did not address state–state forum shopping. In fact, several other Supreme Court cases have accepted forum shopping between different state courts without comment and, in some cases, have even endorsed it.²¹⁹

A second common complaint about forum shopping is that it leads to inconsistent judicial outcomes as litigants seek a more favorable substantive law or a more agreeable decider of the same substantive law.²²⁰ “Forum shopping suggests either a distrust of the [legal] system's capacity to redress wrongs or an effort to obtain more than one's entitlement under the prevailing rules.”²²¹ However, in the American legal system, the political reality is that we shop for law in local legislatures, in Congress, and in the courts.²²² Furthermore, legal decisionmakers, such as judges, lawyers, and legislators are influenced by a variety of factors, both personal and political. Legal outcomes are invariably influenced by these differences.

²¹⁴ See Note, *Forum Shopping Reconsidered*, 103 HARV. L. REV. 1677, 1692 (1990).

²¹⁵ Bassett, *supra* note 205, at 370–73; Note, *supra* note 214, at 1690–91.

²¹⁶ See Note, *supra* note 214, at 1690 nn.99–100.

²¹⁷ 304 U.S. 64, 78 (1938); see Henry J. Friendly, *Averting the Flood by Lessening the Flow*, 59 CORNELL L. REV. 634, 641 (1974).

²¹⁸ See Bassett, *supra* note 205, at 362.

²¹⁹ Note, *supra* note 214, at 1682–83 (giving examples of Supreme Court cases accepting forum shopping); see also Lea Brilmayer & Ronald D. Lee, *State Sovereignty and the Two Faces of Federalism: A Comparative Study of Federal Jurisdiction and the Conflict of Laws*, 60 NOTRE DAME L. REV. 833, 834 (1985) (explaining that state–state forum shopping is a “permissible activity of all shrewd litigants”).

²²⁰ See Kazanoff, *supra* note 76, at 42; Nathan, *supra* note 101, at 113.

²²¹ Note, *supra* note 214, at 1685.

²²² Bassett, *supra* note 205, at 387–88.

A third complaint is that forum shopping creates unnecessary costs and inconvenience for defendants, as it may result in litigation in a forum that is distant from most relevant witnesses and documents. In this regard, note that restrictions on personal jurisdiction limit the number of places where defendants can be sued. Furthermore, procedural rules provide relief if defendants can demonstrate true inconvenience—they can move the court to transfer or dismiss the case under the *forum non conveniens* doctrine or through a motion to transfer venue.²²³ Finally, if the rights that plaintiffs seek to enforce are ones that society values, forum shopping may be socially beneficial because it facilitates the provision of those remedies and results in greater enforcement of the law, even if there is a modest additional expense.²²⁴

One further concern expressed about forum shopping is that it affects a state's ability to be autonomous. "[A] state's choice of policy may be undermined by the ability of litigants to seek a different forum."²²⁵ So, for example, if a state chooses to have a short statute of limitations for certain types of legal claims, but a plaintiff can avoid that statute by filing in a different state, the first state's policies are circumvented. One response to this concern, raised in a civil rights context, is that plaintiffs may view themselves as being part of a larger community than a single state whose claims affect a wider body of citizens.²²⁶ Respecting plaintiffs' alternative permissible choices for filing complaints reflects the values that they are seeking to enforce.

3. *Situating Shareholder Litigation Within the Forum Shopping Debate.*—The forum shopping debate is somewhat different in the context of shareholder representative litigation than in the larger universe of litigation. In an important sense, the space of the debate is narrower. M&A deal litigation cases are usually multijurisdictional filings that all seek to apply the same substantive law, thus eliminating one large reason for forum shopping. No one usually disputes that the law of the state of incorporation (e.g., Delaware) applies to these cases. Rather, the claim seems to be that a non-Delaware court (and possibly jury) is more likely to be overly friendly to plaintiffs, or to a particular plaintiff, in the manner in which it applies Delaware law.²²⁷ "Friendly" in the corporate governance context could

²²³ 28 U.S.C. § 1404 (2006).

²²⁴ See Note, *supra* note 214, at 1692–93; see also George D. Brown, *The Ideologies of Forum Shopping—Why Doesn't a Conservative Court Protect Defendants?*, 71 N.C. L. REV. 649, 671–72 (1993) (describing forum shopping as an acceptable incentive when it comes to furthering societal goals).

²²⁵ Note, *supra* note 214, at 1693.

²²⁶ See *id.* at 1694.

²²⁷ Nathan, *supra* note 101, at 113 (“[P]laintiffs’ lawyers, particularly those with weak cases, hope that other, less experienced judges will misapply Delaware law, that the greater uncertainty of the outcome will increase the settlement value of the litigation . . .”).

mean that the other state has a different view than Delaware as to what breadth of shareholder challenges to management discretion constitutes good corporate policy. If that were the case, we would expect to see correlations between forum selection and such policies, data that has not yet been developed. Plaintiffs continue to file cases in Delaware courts and in the courts of the headquarters state. There have been notable examples of Delaware policies favoring management²²⁸ and the continuing room that the Delaware Supreme Court has given management to use defensive tactics like poison pills.²²⁹ But almost all of the other states quickly followed Delaware's statutory exculpation approach, and some of the larger commercial states have gone beyond Delaware in authorizing anti-takeover defensive tactics and deferring to corporate directors' business judgment.²³⁰

A more refined (or cynical) version of this claim is that plaintiffs file good cases in Delaware and bad cases elsewhere, hoping that the Delaware courts will rule in their favor in strong cases and that other states' courts will not detect the flaws in the weak ones.²³¹ While there is at least superficial plausibility to this claim, it is not without flaws. For one thing, it is an empirical assertion that remains unproven. Furthermore, judges care about the merits of the cases they decide, and it cannot be true that multijurisdictional filings which are based on the same facts, theories, and substantive law are strong in a Delaware court but weak elsewhere. As we discuss below, we believe that there are different forces driving these filings than those commonly associated with forum shopping.

Overall, forum shopping in the corporate setting seems less likely to raise "the spectre of an outcome-altering choice" that often drives forum shopping policy discussion in litigation contexts generally.²³² First, for the reasons noted above, all judges will apply Delaware law and each of the relevant courts have equally valid claims to personal jurisdiction over defendants and subject matter jurisdiction over the case. In terms of venue,

²²⁸ For example, Delaware's legislature effectively overruled the liability-creating rule of *Smith v. Van Gorkom* by enacting a statutory exculpation provision. See DEL. CODE ANN. tit. 8, § 102(b)(7) (2011); see also *Smith v. Van Gorkom*, 488 A.2d 858 (Del. 1985) (holding that directors breached their fiduciary duty in approving a merger, which led to the legislative addition of § 102(b)(7), which permits corporations to exculpate their directors).

²²⁹ See *Versata Enters., Inc. v. Selectica, Inc.*, 5 A.3d 586, 603–06 (Del. 2010) (upholding the legitimacy of a poison pill with a 4.99% trigger).

²³⁰ See, e.g., 15 PA. STAT. ANN. § 1715(b) (West 1995) (directors are not required to regard the interest of any particular group as paramount).

²³¹ Nathan, *supra* note 101, at 113. The claim is that non-Delaware judges will "misapply" Delaware law, systematically leading to greater uncertainty in outcomes and increasing settlement value for some cases. Such claims have yet to be demonstrated empirically. A related claim is that defendants are no longer willing to file motions to dismiss in Delaware because they do not wish to drive deal cases to other forums. See Micheletti & Parker, *supra* note 190, at 12. Cain and Davidoff estimate that "Delaware courts dismiss fewer cases when cases migrate towards other jurisdictions." Cain & Davidoff, *supra* note 36, at 6.

²³² Bassett, *supra* note 205, at 351 (arguing that many such claims are unsubstantiated).

the standard remedy for improper venue is to ask the court to transfer or dismiss the case pursuant to *forum non conveniens*. In almost all cases, the convenience of the parties (e.g., the location of the documents) cuts against Delaware taking these cases and in favor of the defendant's headquarters state. Delaware does have a legitimate argument that it has a strong interest in ensuring that its corporate laws are properly interpreted, a corporate law application of the state-autonomy argument described above. As noted earlier, commentators have observed that Delaware is losing its cases and have raised concerns that this alleged decline could adversely impact Delaware's ability to market its corporate law product.²³³ However, while Delaware's law is as close to a national corporate law as exists, it is plainly not the only state that has an economic interest in the many corporations that are incorporated there but which have their physical operations elsewhere. Particularly in mergers and acquisitions, where the disappearance of a target corporation may have an adverse economic impact on another jurisdiction, it seems odd to say that only Delaware can decide a dispute over the terms of such a takeover. Furthermore, while the Delaware Supreme Court always has the last word on the meaning of its law,²³⁴ the U.S. Supreme Court has not permitted any state to generally exclude another state from hearing cases under the first state's laws for which the other state has jurisdiction.²³⁵

Finally, there are strong reasons to believe that defendants are engaging in forum shopping themselves. Savitt motions, which ask the Delaware court to get all courts with pending litigation to agree to stay their actions in favor of the Delaware forum, are a method of forum shopping.²³⁶ The defendant is trying to ensure that all cases are brought before its preferred forum, the Delaware Chancery Court. At the more extreme end of the spectrum of forum shopping, corporate defendants are adopting bylaw and charter provisions that will ensure that Delaware hears all fiduciary duty cases brought against directors of Delaware corporations, or in some cases, that the board of directors has the power to decide where the case may be brought. This is nothing more than a type of forum shopping by defendants, who are trying to change the rules of the chess game to be more to their liking.

²³³ See *Delaware Cases*, *supra* note 4.

²³⁴ When in doubt, other states' courts can ask the Delaware Supreme Court to determine questions of Delaware law because Delaware's constitution grants that court jurisdiction to hear questions of law certified to it by the highest appellate court of any state. DEL. CONST. art IV, § 11(8).

²³⁵ See *Tenn. Coal, Iron & R.R. v. George*, 233 U.S. 354, 359–60 (1914) (holding Georgia was not bound by the Full Faith and Credit Clause to give effect to an exclusive venue provision); RESTATEMENT (SECOND) OF CONFLICT OF LAWS § 91 (1971).

²³⁶ Defendants are seeking to move the plaintiffs out of their chosen forums into a single court, frequently Delaware. These motions have become increasingly common. C. Barr Flinn & Kathaleen St. J. McCormick, *The Delaware Court of Chancery Endorses One Forum Motions as a Solution to Multijurisdictional Litigation* (Young Conaway Stargatt & Taylor, LLP, Wilmington, Del.), Fall 2001, available at <http://www.youngconaway.com/files/upload/CorporateFall2011.pdf>.

We do not claim that there are no differences between the Delaware courts and other states' courts; rather, our argument is that these differences are not the real drivers of multijurisdictional litigation. As we discuss in the next section, we think other forces are at work.

Moreover, in the end, all of this discussion takes place against the backdrop of a long-running debate over the merits of representative litigation and its value as a constraint on possible abuses of management discretion.²³⁷ Critics label behavior as forum shopping when they want to paint it as unsavory and contrary to public policy, but they avoid that label if they think the reasons for forum selection are reasonable and justified—a difference that often involves a subjective assessment of the litigant's motives.²³⁸ This would not be the first time such claims have been made against shareholder litigation, and, undoubtedly, it will not be the last. Forum shopping principles cannot resolve this issue without bringing in these larger questions of corporate governance.

4. *Fee Distribution Litigation as an Alternative*

Explanation.—Multijurisdictional litigation in shareholder lawsuits raises different, narrower concerns than traditional forum shopping. There are no differences in the underlying legal standards or choice of law rules being used by the different courts hearing these cases. Plaintiffs do not appear to be seeking a friendly jury.²³⁹ Nor is it clear that the Delaware courts either favor or disfavor large attorneys' fees awards for plaintiffs as they have made conflicting statements about this issue.²⁴⁰ While there are some procedural differences between state courts, such as differences in the availability of discovery or ease of scheduling preliminary injunction motions, the traditional concerns about forum shopping do not seem to explain the explosion of this form of litigation.

In this section, we want to offer a somewhat different, and we think more accurate, description of why there has been a large uptick in the number of multijurisdictional cases without a corresponding increase in the number of deals that are attracting litigation. We believe that these suits are really what we will call “fee distribution litigation”—meaning that these cases are filed after suits are filed in another jurisdiction in an effort to give a second set of plaintiffs' law firms a seat at the settlement table and an

²³⁷ *New Look*, *supra* note 5, at 148–65.

²³⁸ Note, *supra* note 214, at 1683–84.

²³⁹ As a court of equity, the Delaware Chancery Court does not permit the possibility of a jury trial, so plaintiffs may forum shop to be in front of a jury, or the threat of a potential jury verdict might provide some leverage to the plaintiffs in settlement negotiations. Michelletti & Parker, *supra* note 190, at 7. Almost no cases go to trial, and current settlement practices do not seem to reflect such a difference. *New Look*, *supra* note 5, at 177 tbl.6 (showing that among all cases resolved at the time of the study, no deal cases went to trial in 1999 and 2000). In other words, there is no evidence that defendants pay a higher price to settle these cases in jurisdictions that might hold a jury trial.

²⁴⁰ See *infra* note 281 and accompanying text.

opportunity to reallocate the pool of attorneys' fees that may be awarded. We argue that fee distribution litigation only requires that the plaintiffs find a court that satisfies the basic jurisdictional and venue requirements for filing and that has a judge who will, at least initially, agree to hear the case even when the defendants argue in favor of dismissal.²⁴¹

We start from the premise that only certain deals are likely to produce settlement and attorneys' fees for plaintiffs' lawyers. As we have shown in other work, the types of mergers and acquisitions transactions that are most likely to attract litigation are large deals, hostile deals, control shareholder squeeze-outs, and deals with cash financing.²⁴² Plaintiffs' law firms file suit on these deals because experience shows that these are the cases most likely to lead to beneficial settlements or at least settlements sufficiently beneficial for a court to award attorneys' fees for bringing the suit. At any given point in time, however, there are only so many of these cases, and, hence, the number of deals that attract litigation (and lead to positive fee awards) is limited. This may explain why the number of deals attracting lawsuits is relatively constant over time in the Cain and Davidoff data.²⁴³

Enter the new, smaller plaintiffs' law firms that we described above.²⁴⁴ These new plaintiffs' law firms can do what all of the other plaintiffs' law firms do and only file suit challenging the deals that other firms challenge. However, they are smaller and less well-known. They are therefore less likely to be one of the plaintiffs' law firm consortiums that are frequently charged with litigating these cases if they are filed, for example, in the Delaware Chancery Court. Delaware's version of the lead plaintiff provision means that the key roles in these representative suits are more likely to go to one (or a few) of the more established and larger plaintiffs' law firms.²⁴⁵ To succeed in the business, new firms must therefore find a way to obtain a slice of the attorneys' fees that are being generated from the limited pool of good, settlement-worthy cases.

As good lawyers, they have determined that they are more likely to be able to control the litigation and potentially get paid if they file suit in a legally acceptable alternative jurisdiction where other law firms have not already done so. Given the jurisdiction and venue rules that we discussed in the previous section, there is almost always at least one other permissible state court where such a suit can be filed and litigated without violating the rules of civil procedure, so long as the judge will, at least initially, permit

²⁴¹ Defendants do not seem to file transfer motions or motions to dismiss in these cases. *See New Look*, *supra* note 5, at 176.

²⁴² *Litigation in Mergers*, *supra* note 5, at 3.

²⁴³ Cain & Davidoff, *supra* note 36, at 31 tbl.1.

²⁴⁴ *See supra* Part I.A.4.a.

²⁴⁵ David H. Webber, *Private Policing of Mergers and Acquisitions: An Empirical Assessment of Institutional Lead Plaintiffs in Transactional Litigation* (July 1, 2012) (unpublished manuscript) (on file with authors).

the plaintiffs to maintain their case if the defendants file objections. If the larger, more established plaintiffs' law firms choose to file suit in Delaware, the state of the target company's incorporation, then the new kids on the block can bring their action in the courts of the state in which the target company is headquartered.²⁴⁶ This would explain the observed big increase in multijurisdictional litigation.

However, there is one more step in the process: the new firms need to have some way to force defendants to include them in any settlement that they reach with the older, more established firms. Let us add to the mix, then, the fact that defendants generally insist on global settlements of all litigation related to a common fact pattern, whether it is filed in one court or many, and whether it is deal-related or a derivative claim.²⁴⁷ In a global settlement, the defendant gets a release of all claims, actual or potential, that could be brought by the shareholders of the company in any forum. In our example, this means that the defendants will want to settle the litigation in both jurisdictions—the state of incorporation and the state of headquarters—to be assured that any settlement will finally put to rest all possible claims in the various cases. This is what gives the new firms leverage to get themselves included in the settlement negotiations: if the older plaintiffs' firms do not include them, then they can refuse to settle their cases, or even worse, offer to settle them more cheaply in a reverse auction.²⁴⁸ Facing this threat, and knowing that the defendants will not agree in most circumstances to partial settlements, the older firms are forced to negotiate with the newer ones over the allocation of attorneys' fees in any settlement.

5. *The Costs and Benefits of Fee Distribution Litigation.*—On balance, is fee distribution litigation harmful? There are at least two kinds of benefits that are created by this form of multijurisdictional litigation. First, it preserves the traditional jurisdictional and venue rules for forum selection that apply in all other areas of the law. To return to our earlier chess analogy, it still allows white to move first in any manner permitted by the rules of the game. Second, this form of litigation preserves other states' ability to influence the business and affairs of corporations headquartered in their states. As the law stands today, the Delaware courts have a quasi-monopoly over the future growth of the corporate law that affects public companies. There are some advantages to this quasi-monopoly, such as predictability and certainty of outcome in most cases provided by judges with expertise. Yet, one does not have to believe in the race to the bottom to

²⁴⁶ This process could be reversed if the larger, better established firms select the target's headquarters state as their preferred forum, thus leading the smaller firms to go to the courts of the state of incorporation. However, the scenario described in the text is traditionally the more common one.

²⁴⁷ See Kazanoff, *supra* note 76, at 43 (“[D]efense counsel almost always assert the ‘all-we-care-about-is-one-forum position’ . . .”); Michelletti & Parker, *supra* note 190, at 12 n.41.

²⁴⁸ See discussion *infra* Part II.C.1.

see that there can be too much of a good thing. Multijurisdictional litigation gives other states' courts a channel to articulate their states' interests in these cases.

What about the costs? We note first that the defendants' costs for settling these cases appear relatively unaffected.²⁴⁹ A substantial number of shareholder litigation cases are dismissed with no settlement and very little litigation activity.²⁵⁰ Almost all of the settlements reported by Cain and Davidoff are based on increased disclosures being made to the class of affected shareholders, so that any direct costs from these settlements (such as greater deal-consideration payments) are unlikely solely because more cases arising out of the same transaction are settled at the same time.²⁵¹ As to plaintiffs' attorneys' fee awards,²⁵² multijurisdictional global settlements could conceivably cost defendants more than settlements in one court, but they may not; defendants will push back against paying more. It is also possible that more suits would generate more instances in which attorneys' fees are paid with no benefit to shareholders, a traditional concern of those worried about strike suits, but the studies of the increase in multijurisdictional litigation have not yet shown that.²⁵³ Instead, what we do see is litigation to shape how the plaintiffs' attorneys' fee award will be divided amongst the plaintiffs' law firms that are engaged in the litigation. While the answer to this question matters a lot to those firms, it is of much less concern to society and would need to be balanced by the possible deterrence of meritorious suits because other plaintiffs could free ride on the work done by one plaintiffs' firm, thereby reducing the first firm's incentives. Certainly, any solution to this distributional problem should not be an expensive and difficult one to implement.

To finish the social welfare analysis, we need to examine whether these extra cases arising out of the same transaction result in duplicative discovery costs and duplicative motions resolved at the cost of judicial resources and attorney time. The best empirical evidence is from the deal cases and shows that not much discovery is taken in most deal cases and few pretrial dispositive motions are filed and briefed.²⁵⁴ Moreover, if

²⁴⁹ We are not claiming that there are no costs associated with multijurisdictional litigation. For example, Cain and Davidoff provide some evidence that Delaware has a higher dismissal rate than other jurisdictions, but that it dismisses fewer cases when they are filed in multiple jurisdictions. See Cain & Davidoff, *supra* note 36, at 5–6. If other states are not dismissing these cases, then there may be more cases settled, which, all other things being equal, could raise the defendants' litigation-related costs.

²⁵⁰ *New Look*, *supra* note 5, at 176, 189.

²⁵¹ Cain & Davidoff, *supra* note 36, at 33 (finding that some settlements do involve an increase in the deal consideration, but that there is no evidence that the amount of the increase depends on the number of cases being settled).

²⁵² As we noted earlier, there is no publicly available information about defendants' attorneys' fees that would allow us to make any factual determination about changes to them.

²⁵³ Cain and Davidoff's data are the best available at this point, but they do not establish any causal relationship between multijurisdictional litigation and weaker cases being filed.

²⁵⁴ *New Look*, *supra* note 5, at 189.

discovery practice is de facto to conduct all discovery on a consolidated basis across jurisdictions, and only one preliminary injunction motion is scheduled per transaction, then the cost increases associated with multijurisdictional litigation, while positive, may be relatively small. And last but not least, we must consider the court's time and efforts: with multijurisdictional litigation, more than one court must be involved in every case, and this undoubtedly imposes some costs on the judiciary. However, most of the time, judges are not being asked to decide weighty issues of corporate law, or even of civil procedure, but rather to manage some preliminary discovery motion practice and to resolve law firm jockeying for lead positions in the litigation.²⁵⁵ Relatively few judicial resources are likely to be expended in this type of work, and those resources are being provided by courts in other states that are willingly choosing to assume jurisdiction over a case that could otherwise be litigated in Delaware.

To sum up, this type of litigation is different because it is largely about dividing up the attorneys' fee awards that are made in a limited number of settlement-worthy cases. For that reason, we think that the new multijurisdictional cases being filed are best described as fee distribution litigation. They do not contribute much to the resolution of the main cases being filed, nor do they appear to generate much in the way of additional costs.²⁵⁶ We agree, therefore, with the mainstream belief that there is a problem here that needs to be addressed, but we disagree with most of that commentary about the size of the problem. Based on the existing evidence, we believe that the costs associated with this new form of multijurisdictional litigation are relatively small and therefore that only relatively inexpensive, limited solutions should be adopted. In the next section, we survey the possible policy solutions.

C. Current Proposals for Fixing the Problem

Based on the forgoing discussion, we think that fee distribution litigation may impose limited social costs and somewhat greater private costs, particularly on larger, more established plaintiffs' firms. Various possible solutions exist, some resting on judicial actions and others looking to legislative action or private ordering. In this section, we evaluate six solutions in light of two major lessons from the previous Parts: first, that the empirical evidence seems to point not so much to an increase in strike suits, but instead to a jump in multidistrict litigation seeking a share of the attorneys' fees arising from suits with some merit, and second, that broader jurisdictional and procedural policies limit some of the solutions proposed.

²⁵⁵ As noted above, deal cases do not involve many substantive motions and are resolved quickly. *See id.* at 176, 189.

²⁵⁶ We caution that there is more work to be done to empirically document what are the extra costs associated with multiple lawsuits being filed in different courts for each transaction and when such additional costs are material.

1. *Matsushita, Reverse Auctions, and Collateral Attacks.*—The lure of obtaining the first settlement among multiple suits arising out of the same action looms large in the practicality of representative litigation. After *Matsushita*, the first lawyer to achieve a global settlement can effectively block suits by other firms seeking to represent the class. A law firm unable to participate in the litigation in the initial jurisdiction (e.g., by not being selected as lead plaintiff or as part of the steering committee for that litigation) has an incentive to file in a second jurisdiction to gain control of the litigation or to obtain a seat at the settlement table when fees are being negotiated. Professor Coffee's writing on "reverse auctions" describes how defendants can force plaintiffs that have filed competing actions arising out of the same transaction to bid against one another to settle the case most cheaply.²⁵⁷ By doing so, the class action defendant seeks to secure a global settlement for as little as possible. However, this also has an indirect effect of reducing plaintiffs' lawyers' incentives to aggressively litigate in the first place because a firm that invests a lot in developing a case risks seeing the fruits of its labor expropriated by a low-cost, free-riding firm that is willing to settle the case for less.²⁵⁸

On remand, the Ninth Circuit in *Matsushita II* provided one response to the problem, denying finality if there is a constitutional defense such as lack of adequate representation.²⁵⁹ The Ninth Circuit allowed the absent members of the class to claim that they were inadequately represented by the settling attorneys.²⁶⁰ While some scholars favor this approach,²⁶¹ others have been critical of it, claiming that it leads to excessive litigation.²⁶²

²⁵⁷ *Class Wars*, *supra* note 81, at 1370.

²⁵⁸ Some commentators have urged courts to split plaintiffs' attorneys' fees equitably (recognizing that often the attorneys who do most of the research and litigate the most aggressively are undercut by others looking for a quick settlement and that such an outcome is inequitable). See Marcel Kahan & Linda Silberman, *The Inadequate Search for "Adequacy" in Class Actions: A Critique of Epstein v. MCA, Inc.*, 73 N.Y.U. L. REV. 765, 784 (1998).

²⁵⁹ *Epstein v. MCA, Inc. (Matsushita II)*, 126 F.3d 1235, 1251 (9th Cir. 1997), *withdrawn and superseded on reh'g*, 179 F.3d 641 (9th Cir. 1999).

²⁶⁰ *Id.*; see also Alexandra Lahav, *Fundamental Principles for Class Action Governance*, 37 IND. L. REV. 65, 94 (2003) ("Of the proposals put forward, the one most consistent with accepted attorney compensation norms is to link attorneys' fees to the amount of benefit the attorney provides the class . . .").

²⁶¹ See David A. Dana, *Adequacy of Representation After Stephenson: A Rawlsian/Behavioral Economics Approach to Class Action Settlements*, 55 EMORY L.J. 279, 321–22 (2006) (suggesting that the collateral attack mechanism encourages more productive bargaining between the parties at the onset of the settlement process because they know that the settlement can be attacked later if inadequate).

²⁶² Kahan & Silberman, *supra* note 258, at 784 ("[T]he collateral attack remedy created by *Matsushita II* entails substantial costs. Recall, in this respect, the breadth of the remedy: A collateral attack appears to be available without a threshold showing that forum shopping has in fact occurred . . ."); see also Issacharoff & Nagareda, *supra* note 49, at 1669 (noting that the court invalidating the settlement may be anomalous or, "to put the point another way, what if the second forum is the product of the same type of forum shopping, only this time on behalf of an improperly motivated attack on a well-considered class settlement?"). But see Patrick Woolley, *The Availability of Collateral Attack for Inadequate Representation in Class Suits*, 79 TEX. L. REV. 383, 443 (2000)

Professors Issacharoff and Nagareda argue for a more limited collateral attack, available only in strategically filed cases.²⁶³ Under their proposal, cases could only be reopened under Federal Rule of Civil Procedure 60(b), which would allow for a change due to, for instance, new evidence or mistake by counsel.²⁶⁴ After the review under Rule 60(b), collateral attack would be semi-precluded for structural issues, dealing with the bargaining but not the substance of the deal. Preclusion would turn on “the rigor of the rendering court’s determination of the structural question”; if the original court made a “reasoned determination,” then the attack is precluded.²⁶⁵ Collateral attack would be precluded for “performance defects” (i.e., a bad settlement but not an unfair one), as long as the party had a chance to object in the original court.²⁶⁶

Other proposals have focused on adjusting attorneys’ fees under *Matsushita* to mute the incentives imposed by finality.²⁶⁷ Overall, this approach is a very litigation-intensive solution, requiring a case-by-case determination on a factually intense basis. Plaintiffs who did not get attorneys’ fees would be the ones bringing the case, in effect requiring them to double down their investment on a lawsuit that would have not yet provided any return.

2. *Judicial Cooperation and Comity*.—Judicial comity is an alternative, judicially based solution that could, unlike the approaches just discussed, address these issues before a case is heavily litigated. Beginning in the early 2000s, when the problem of multijurisdictional litigation in M&A litigation first emerged, Chancellor William Chandler of the Delaware Chancery Court developed a practice of pursuing judicial comity.²⁶⁸ Initially on a *sua sponte* basis,²⁶⁹ but later in response to a Savitt

(“Notwithstanding the longstanding availability of collateral attack, such attacks have not been common, suggesting that there is no basis for alarmist predictions.” (footnote omitted)).

Kahan and Silberman also argue that the Ninth Circuit’s decision undercuts the policy behind the Full Faith and Credit Act. See Kahan & Silberman, *supra* note 258, at 785 (arguing that the Full Faith and Credit Act is based on a policy of finality, and that allowing collateral attacks on adequacy of representation inevitably goes against finality as it allows cases to be relitigated in other fora).

²⁶³ Issacharoff & Nagareda, *supra* note 49, at 1655.

²⁶⁴ *Id.* at 1711–12. However, Federal Rule of Civil Procedure 60(b) only allows for review in the same forum that the original case was filed in, removing the possibility of forum shopping. *Id.* Issacharoff and Nagareda note the availability of malpractice actions against the lawyers that negotiated the bad settlement, but also acknowledge that, to proceed on a malpractice action, the plaintiff must recognize that the settlement is binding, something many plaintiffs are unwilling to do given other alternatives. *Id.* at 1712.

²⁶⁵ *Id.* at 1716–17.

²⁶⁶ *Id.* at 1719.

²⁶⁷ See Kahan & Silberman, *supra* note 258, at 778; Lahav, *supra* note 260, at 93–95.

²⁶⁸ E-mail from Chancellor William Chandler to Randall Thomas (July 21, 2011) (on file with authors).

²⁶⁹ Chancellor Chandler would only proceed if counsel for the parties were in agreement with this approach. *Id.*

motion,²⁷⁰ Chandler would contact the other judge(s) in courts with pending litigation from the same transaction and discuss which forum was the most appropriate for the litigation to proceed. For example, in *Nierenberg v. CKx, Inc.*,²⁷¹ plaintiffs filed cases arising out of the same transaction in Delaware before Chancellor Chandler and in New York before Judge Ramos of the New York Supreme Court.²⁷² The two judges agreed that it was duplicative for both matters to proceed and ultimately determined that the two cases should be consolidated in Delaware, after which the New York plaintiffs voluntarily stayed their case and joined in the Delaware litigation.²⁷³

The attraction of judicial comity is that it can be implemented without any changes to the existing litigation system and, if practiced effectively by judges and agreed to by counsel, will result in all cases arising out of the same transaction being litigated in one forum.²⁷⁴ Well-intentioned judges can effectively weigh factors such as their courts' respective docket delays, their expertise in deciding corporate law issues, the quality of the cases filed in their jurisdiction, the qualifications of the attorneys pursuing the matter, the consent of the attorneys involved, and the strength of their jurisdiction's interest in a corporation's affairs in determining which court is most appropriate to handle the case. As practiced by Chancellor Chandler, judicial comity has been an efficient mechanism for reallocating these cases between state courts without demanding too much of their time. Moreover, practitioners think that it works well most of the time.²⁷⁵

Nevertheless, there are some drawbacks to this approach. First, one can easily imagine that not all judges, nor all attorneys, will be willing to participate in this process. Because it is an informal, judge-driven solution, the potential for defections is significant, and there is no policing mechanism.²⁷⁶ Moreover, even judges that participate may have incentives

²⁷⁰ *Id.* A Savitt motion, named after Bill Savitt of the firm of Wachtell, Lipton, Rosen & Katz, is a motion filed by the defendants in M&A litigation asking the competing courts with litigation based on the same transaction to reach a decision about the appropriate forum for the case. See Flinn & McCormick, *supra* note 236, at 5 n.2.

²⁷¹ Nos. 5545-CC, 6519-CC, 6524-CC, 2011 WL 2185614 (Del. Ch. May 27, 2011).

²⁷² *Id.* at *1.

²⁷³ *Id.* at *2. Ultimately, Chancellor Chandler applied the *Hirt* factors, discussed below, to determine the lead counsel structure of the Delaware case. See *id.* at *2 & n.7.

²⁷⁴ Federal courts may be able to do the same in a somewhat different manner: a federal court could abstain under the Colorado River doctrine from hearing federal proxy claims and breach of fiduciary duty claims in favor of a Delaware action raising similar claims under Delaware law. See, e.g., Micheletti & Parker, *supra* note 190, at 45.

²⁷⁵ Micheletti & Parker, *supra* note 190, at 16–17 (“By and large, such motion practice has been successful . . .”).

²⁷⁶ Although the judicial clerkship application process is quite different, it provides an excellent illustration of the difficulty of getting judges to abide by self-imposed rules when they perceive advantages in defecting from them. See, e.g., Catherine Rampell, *Judges Compete for Clerks on Lawless Terrain*, N.Y. TIMES, Sept. 24, 2011, at B1 (discussing judicial rebellion from the clerkship hiring plan).

to divert cases to inefficient jurisdictions. For example, presiding over high-profile cases may provide some judges with significant psychological benefits, perhaps because of favorable press coverage (especially for elected judges) or a greater sense of personal importance. Finally, judges may simply disagree about the proper forum for a case even after exerting great efforts to reach a successful resolution. In this event, unless one judge is willing to concede the point, there will still be more than one forum where the litigation proceeds.

Assessing the value of judicial comity as a solution to the multijurisdictional litigation problem requires a careful cost-benefit analysis. We think that it is a relatively low-cost, easily reversible policy approach that has the great virtue of not requiring any dramatic (and untested) changes to the existing judicial system's treatment of representative litigation. It has great flexibility, as it is a case-by-case approach that permits judges to carefully weigh the respective interests of their jurisdiction and its corporations in having the litigation resolved in their court. For example, a California court and a Delaware court could well conclude that a Delaware corporation with its headquarters in California, all of the potential witnesses and documents in that state, and all of its investors located there, was better served by having the case litigated in California rather than Delaware. If, as we suggest here based on current empirical evidence,²⁷⁷ multijurisdictional litigation is a much less costly problem than some lawyers claim, then this low-cost and easily reversible solution is the best one to implement at this time.²⁷⁸

3. *Reforms to Increase Monitoring of Attorneys' Fees.*—If forum shopping is often the result of poorly monitored class counsel taking self-serving actions, then one solution could be for state courts to implement measures to improve the class representatives' incentives to monitor their attorneys.²⁷⁹ The lead plaintiff provision that was added to the federal securities laws in 1995 has been the most notable recent reform, but it does not apply to the bulk of state litigation.²⁸⁰

Delaware judges have been outspoken in recent years about their perceptions of class counsel's abuses in the deal litigation process. For

²⁷⁷ If new empirical evidence becomes available that indicates the problem has become more costly, then we would need to revisit this issue.

²⁷⁸ To the extent that other states' courts face novel issues of Delaware law, they would be able to certify them to the Delaware Supreme Court under the terms of the Delaware constitution. DEL. CONST. art. IV, § 11(8).

²⁷⁹ See, e.g., *In re Del Monte Foods Co. S'holders Litig.*, C.A. No. 6027-VCL, slip op. at 8–9, 17 (Del. Ch. Dec. 31, 2010) (noting that “clients can and should . . . closely monitor[] the actions of their attorneys” and highlighting congressional measures to incentivize increased monitoring (citing *New Look*, *supra* note 5, at 148)); *In re Revlon, Inc. S'holders Litig.*, 990 A.2d 940, 960 (Del. Ch. 2010) (discussing self-serving behavior of class counsel).

²⁸⁰ See James D. Cox & Randall S. Thomas, *Does the Plaintiff Matter? An Empirical Analysis of Lead Plaintiffs in Securities Class Actions*, 106 COLUM. L. REV. 1587, 1588–89 (2006).

example, Chancellor Strine has been blunt in his critique of class counsel in some matters.²⁸¹ Perhaps as a result, the Delaware Chancery Court moved to implement a form of lead plaintiff provision.²⁸² The leading case, *Hirt v. United States Timberlands Service Co.*,²⁸³ provides a six-factor test for determining lead plaintiffs.²⁸⁴ While the multifactor test makes Delaware's approach broader and more nuanced than the federal approach,²⁸⁵ the federal approach of preferring the largest investor, expressed in Delaware as "relevant economic standing," is one of the most important of Delaware's factors. After some initial back and forth between members of the court,²⁸⁶ Chancellor Chandler and Vice Chancellor Laster appeared to agree that the significance of the plaintiff having a substantial economic stake is that it

²⁸¹ See *In re Cox Commc'ns, Inc. S'holders Litig.*, 879 A.2d 604, 622 (Del. Ch. 2005) (stating that the counsel had dubious incentives); see also Transcript of Courtroom Status Conference at 18–20, *Scully v. Nighthawk Radiology Holdings, Inc.*, C.A. No. 5890-VCL (Del. Ch. Dec. 17, 2010).

²⁸² The Court has stated a preference that class action plaintiffs agree on a lead plaintiff and counsel without involving the Court, but nevertheless has been willing to develop the *Hirt* test. See *Hirt v. U.S. Timberlands Serv. Co.*, C.A. No. 19575, 2002 WL 1558342 (Del. Ch. Jul. 3, 2002); see also *In re Revlon*, 990 A.2d at 955 ("On those occasions when this Court has been forced to choose among competing candidates for lead counsel, our decisions have stressed the importance of [the *Hirt*] factors . . ." (emphasis added)); *Wiehl v. Eon Labs*, C.A. No. 1116-N, at 10, 2005 WL 5755542, at *5 (Del. Ch. Mar. 22, 2005) (ordering plaintiffs' counsel to convene and determine a litigation structure); *TCW Tech. Ltd. P'ship v. Intermedia Commn'cs, Inc.*, C.A. Nos. 18336, 18289, 18293, at 7–8, 2000 WL 1654504, at *3 (Del. Ch. Oct. 17, 2000) ("In every single instance that I am able to recall, this Court has resisted being drawn into [disputes about coordinating the prosecution of shareholder litigation].").

²⁸³ 2002 WL 1558342, at *2. *Hirt* heavily relied on the *TCW* decision for the first five factors and added a sixth in reliance on Court Rule 23(a)'s focus on competence and resources of counsel. *Id.* The factors are: (1) "the quality of the pleading that appears best able to represent the interests of the shareholder class and derivative plaintiffs; [(2)] the relative economic stakes of the competing litigants in the outcome of the lawsuit (to be accorded 'great weight'); [(3)] the willingness and ability of all the contestants to litigate vigorously on behalf of an entire class of shareholders; [(4)] the absence of any conflict between larger, often institutional, stockholders and smaller stockholders; [(5)] the enthusiasm or vigor with which the various contestants have prosecuted the lawsuit; [(6)] competence of counsel and their access to the resources necessary to prosecute the claims at issue." *Id.* (footnotes omitted).

²⁸⁴ *Id.*; see also *King v. Verifone Holdings, Inc.*, 12 A.3d 1140, 1151 (Del. 2011) (noting the purpose and use of considering various factors to select both lead counsel and lead plaintiffs); *In re Del Monte*, C.A. No. 6027-VCL, at 22 (applying the *Hirt* factors to determine whether counsel would effectively represent the class); *In re Revlon*, 990 A.2d at 955 (discussing the court's reliance on "factors that will lead to meaningful representation").

²⁸⁵ See *In re Del Monte*, C.A. No. 6027-VCL, at 10 ("The *Hirt* factors contemplate a more nuanced and case-specific test [than the federal test] in which the Court examines both the proposed lead counsel and the proposed named plaintiff."). The Delaware approach also avoids a bright-line rule. *Id.*

²⁸⁶ Originally, Chancellor Chandler in *TCW* thought that "the Court should give weight to the shareholder plaintiff that has the greatest economic stake in the outcome of the lawsuit." *TCW*, 2000 WL 1654504, at *4. In 2002, Vice Chancellor Lamb held in *Hirt* that the relative economic stakes should be given great weight. See *Hirt*, 2002 WL 1558342, at *2. The Vice Chancellor explained in *Wiehl* that great weight should be given to the examination of relative economic stakes as a share of the company's total outstanding stock. See *Wiehl*, 2005 WL 5755542, at *3. Because each plaintiff's "respective stakes in [the company was] miniscule," Vice Chancellor Lamb saw no "substantial relative difference." *Id.* In *Dutiel*, Chandler indicated that *Wiehl* confused relative with absolute. *Dutiel v. Tween Brands, Inc.*, C.A. Nos. 4743-CC, 4845-CC, 2009 WL 3494626, at *2–3 (Del. Ch. Oct. 28, 2009). Ultimately, Chancellor Chandler concluded that focusing on only relative or only absolute economic stakes can undermine the analysis. *Id.*

“provide[s] an economic incentive to monitor counsel and play a meaningful role in conducting the case.”²⁸⁷ In *Hirt*, the plaintiff with a greater economic stake in the case’s outcome prevailed as lead plaintiff, but none of the other factors entered into the court’s decision, nor did they receive much discussion.²⁸⁸

While size of economic stake should be an important factor,²⁸⁹ other aspects of the test highlight useful additional concerns. For example, one valuable aspect of the *Hirt* test is its concern with quality of representation: better quality law firms should do a better job of representing the shareholder class.²⁹⁰ Moreover, by rejecting the first-in-time rule for the selection of lead counsel, the *Hirt* factors discourage hasty filings and subpar prosecution of the suit.²⁹¹ Furthermore, because it includes a number of factors pertaining to plaintiffs’ counsel and their prior behavior in the litigation, the *Hirt* test ensures a comprehensive, nuanced approach. Judges can consider any facts they deem relevant to selecting the plaintiff and law firm most likely to achieve the best result for the plaintiff class as a whole. In *Del Monte*, for instance, a potential class representative, Union, held a \$36 million investment in the defendant, by far the largest stake of any of the plaintiffs.²⁹² But because Union faced a potential standing issue, Vice Chancellor Laster determined that the expedited schedule demanded that the case avoid “side issues” and held that the standing issue was a conflict of interest under factor four.²⁹³

²⁸⁷ *In re Revlon*, 990 A.2d at 955. In *Del Monte*, Laster quotes that language and clarifies that a plaintiff must have a “sufficiently large stake to provide incentive to monitor counsel and reduce agency costs.” *In re Del Monte*, C.A. No. 6027-VCL, at 11–12 (dismissing lead plaintiff classification for a plaintiff with only \$7000 in holdings and finding that a \$36 million holding is more significant than a \$475,000 holding). Vice Chancellor Laster’s analysis looked to plaintiff’s overall holdings in the company, as well as to the share those holdings represented in each plaintiff’s portfolio. *Id.* In *Dutiel*, Chandler suggested that the court consider the economic stakes and identities of the plaintiffs to determine their incentive to “participate in the litigation and monitor his or her counsel.” 2009 WL 3494626, at *3.

²⁸⁸ 2002 WL 1558342, at *3.

²⁸⁹ Transcript of Oral Argument on Competing Motions for Appointment of Colead Plaintiffs and Colead Counsel and Class Certification and Rulings of the Court at 76, *In re Medco Health Solutions, Inc. S’Holders Litig.*, C.A. No. 6720-CS (Consolidated) (Del. Ch. Aug. 23, 2011) (“If I have to decide on the groups as proposed, I, frankly, go with the group with the larger shares in terms of the collective track record of those involved in this area of law.”).

²⁹⁰ In the words of one prominent plaintiffs’ attorney, “the quality of pleadings factor is a proxy for who has done the most work leading up to the lead counsel fight and who is likely to be the best lawyer for the class.” Interview by Randall Thomas with plaintiffs’ lawyer (Jan. 31, 2012).

²⁹¹ 2002 WL 1558342, at *2 (“[N]o special weight or status will be accorded to a lawsuit ‘simply by virtue of having been filed earlier than any other pending action.’” (quoting *TCW*, 2000 WL 1654504, at *3)); see also *In re Revlon*, 990 A.2d at 959 (“[A] systemic problem emerges when entrepreneurial litigators pursue a strategy of filing a large number of actions, investing relatively little time or energy in any single case, and settling the cases early to minimize case-specific investment and maximize net profit.”); *Hirt*, 2002 WL 1558342, at *2 (factors one, five, and six).

²⁹² *In re Del Monte*, C.A. No. 6027-VCL, at 11.

²⁹³ *Id.* at 13–15.

Although the *Hirt* test is the established mode of analysis in the Delaware Chancery Court,²⁹⁴ the inquiry is fact driven and thus varies from case to case.²⁹⁵ In addition, Vice Chancellor Laster articulated three categories of *Hirt* factors in *Del Monte*²⁹⁶: lead plaintiff factors, counsel's performance in the litigation to date, and counsel's track record and ability to litigate going forward. Although no other chancery court judge has applied these factors yet, if the goal is to ensure effective representation of the class, these additional categories should be considered carefully as a supplement to the *Hirt* analysis.

This form of innovative state court action could address perceptions that representative litigation faces high agency costs. It works well when multiple cases are filed within the same jurisdiction, yet there is no effective mechanism for implementing it across jurisdictions.²⁹⁷ Even worse, any state that pursues such a course of action unilaterally may find that it has driven representative litigation out of its courts, or more likely, that even though it has improved the alignment between counsel and clients for cases in its own courts, the attorneys it did not select to be lead counsel still file their cases in another state's courts. In other words, coordinated state action is needed to ensure that innovative techniques for reducing litigation agency costs are broadly adopted. While such coordination would be most effective if it included all states, given that most cases are filed either in the headquarters state or state of incorporation of the defendant corporation, even agreement only among the major commercial states would be largely effective.²⁹⁸

²⁹⁴ *Hirt* has been applied in subsequent Delaware Chancery Court cases, but does not seem to have been adopted by the Delaware Supreme Court. The Delaware Supreme Court in *King* merely cites *Hirt* in passing, alongside *Dutiel*, which lists three *Hirt* factors. See *King v. Verifone Holdings, Inc.*, 12 A.3d 1140, 1151 & n.66 (Del. 2011) ("Both Delaware and federal courts generally consider various factors when selecting lead plaintiff (and lead counsel), the goal being to appoint the representative who will best serve the interests of the corporation and its shareholders and most effectively prosecute the litigation.").

²⁹⁵ For example, the *Del Monte* court thoroughly discussed all six factors individually before reaching its decision, see *In re Del Monte*, C.A. No. 6027-VCL, at 11–22, whereas in *Wiehl*, the court only discussed the factors in dispute by the competing plaintiffs' firms, see *Wiehl v. Eon Labs*, C.A. No. 1116-N, 2005 WL 5755542, at *5 (Del. Ch. Mar. 22, 2005) (noting that the remaining *Hirt* factors are no less important). Similarly, the *Dutiel* court stressed that "[Delaware] precedent clearly holds that the Court should consider several factors when deciding which plaintiff the Court will appoint as lead plaintiff." *Dutiel v. Tween Brands, Inc.*, C.A. No. 4743-CC, 2009 WL 3494626, at *3 (Del. Ch. Oct. 28, 2009).

²⁹⁶ *Del Monte*, C.A. No. 6027-VCL, at 11–21. The Vice Chancellor applied the *Hirt* factors in *In re Mosaic Co. Shareholder Litigation*, C.A. No. 6228-VCL (Del. Ch. Mar. 14, 2011).

²⁹⁷ Professor Quinn's suggestion of an interstate MDL panel might be another potential state law innovation that could effectively address litigation agency costs, if it could be implemented politically. See Quinn, *supra* note 4, at 162.

²⁹⁸ We note that public corporations that do not elect to incorporate in Delaware almost always incorporate in the state of the company's headquarters. See *Bebchuk & Cohen*, *supra* note 138, at 383–84 (discussing factors that motivate incorporation choices). This means that there is generally only one state court venue option for representative suits against companies from these states.

4. *Providing a Federal Forum for Representative Litigation.*—One way to overcome this state-coordination problem would be through federal legislation. Existing federal law already provides a federal forum when there is reason not to trust state courts, as in the context of a plaintiff litigating in courts of the defendant’s home state, even though the substance of the home state’s law continues to be applied in the federal court. The Class Action Fairness Act, federal legislation passed in 2005, expanded that policy to provide a federal forum for any large class action arising under state law.²⁹⁹ That legislation, however, contains a Delaware carve out that preserves state court jurisdiction for matters of corporate governance and internal corporate affairs, which would cover all of the state law actions described in Part I.

One option for resolving the problems related to multijurisdictional litigation would be to force mergers, class actions, and derivative suits to be heard in federal court where existing processes for multidistrict litigation could be used for dealing with multiple filings.³⁰⁰ Effectively, the existence of the MDL panel sharply reduces the incentives that attorneys might otherwise have to engage in forum shopping in order to take advantage of perceived differences in the way that different courts may decide cases and leads to more rational filing patterns.³⁰¹

As part of federalization, Congress could choose to impose other litigation agency-cost-reducing requirements on state law mergers and acquisition class actions and derivative lawsuits.³⁰² One of the PSLRA’s main features was the lead plaintiff provision, which created a presumption that the plaintiff with the largest financial stake in the litigation should be appointed the lead plaintiff.³⁰³ The lead plaintiff requirement has had several beneficial effects on federal securities class actions, including increased shareholder monitoring of class counsel, greater involvement of institutional investors, and higher settlements when institutional investors become involved.³⁰⁴ While Delaware has moved in this direction in recent years with the promulgation of the *Hirt* test, to date no other states have

²⁹⁹ 28 U.S.C. § 1332(d)(9)(B) (2006).

³⁰⁰ See *id.* § 1407. Although technically this only pertains to pretrial matters, as a practical matter a high percentage of these transferred cases are decided by the transferee court through some form of pretrial disposition. Patricia D. Howard, *A Guide to Multidistrict Litigation*, 124 F.R.D. 479, 480 (1989) (finding that only 18% of cases were remanded to their original court).

³⁰¹ See Cox et al., *supra* note 77, at 443–44 (finding that most securities fraud class actions are filed in the home circuit of the defendant corporation).

³⁰² See Johnson, *supra* note 3, at 385–86; Comm. on Sec. Litig., Ass’n of the Bar of the City of New York, *Coordinating Related Securities Litigation: A Position Paper 9–10* (2008), available at www.nycbar.org/pdf/report/Securities_Litigation_%20A.pdf.

³⁰³ 15 U.S.C. § 78u-4(a)(3) (2006).

³⁰⁴ Cox & Thomas, *supra* note 280, at 1596–97; James D. Cox et al., *There Are Plaintiffs and . . . There Are Plaintiffs: An Empirical Analysis of Securities Class Action Settlements*, 61 VAND. L. REV. 355, 385 (2008).

adopted similar requirements. Federalization could impose such a requirement nationally.³⁰⁵

This result, however, seems the worst kind of compromise. The substantive law would remain as set by the state legislature, for example, the Delaware General Corporation Law, but litigation could occur in front of hundreds of federal district judges spread around the country who seldom are repeat players in corporate law. It seems logical that, as a general matter, state courts should be better than federal courts at interpreting state law, especially if the state courts are specialized business courts interpreting their own state's corporate law. It also seems like overkill to federalize the entire field of state corporate law to solve the problem of forum shopping in representative litigation. Furthermore, state courts can find ways to reduce litigation agency costs when they believe action is needed.³⁰⁶ We would lose most of the advantages of the current Delaware-centric corporate law system with few countervailing advantages.

The Delaware court system has long been a key part of the Delaware corporate law product. If Congress were to go this far, why would they not want to take the then seemingly small additional step of federalizing the substance of corporate law? Federal preemption of state corporate law is a heavily debated topic,³⁰⁷ and we are disinclined to spill more ink in the debate here, but it would seem truly bizarre if, after not enacting federalization at any time over the last eighty years, Congress were to choose to do it via a procedural change.

5. *Coordinating State Action on Multijurisdictional Litigation.*—As an alternative to federal imposition of a common forum or rule coordinating cases, states could coordinate among themselves on lead plaintiff provisions, an MDL process, or an exclusive forum provision. The Model Business Corporation Act (MBCA), a seven-decade-long project of a committee of the American Bar Association, already provides the basis for the corporate law in more than 60% of the states (once enacted by the legislatures of those states). As such, it would be a logical focal point for such legislation.³⁰⁸ Delaware, the home of more than 50% of America's

³⁰⁵ Alternatively, Congress might restrict the carve out to cases filed in the corporation's state of incorporation, in most cases Delaware, out of respect for the quality of the Delaware courts in the corporate law arena. See Johnson, *supra* note 3, at 386. However, we note that for federal securities fraud class actions, plaintiffs' counsel overwhelmingly choose to file in the headquarters state of the defendant corporation, which is likely to be the most convenient forum for the defendants. See Cox et al., *supra* note 77, at 443 tbl.3 (84% of federal securities class actions are filed in the circuit containing the defendant corporation's headquarters).

³⁰⁶ See *supra* Part II.C.3.

³⁰⁷ See, e.g., Mark J. Roe, *Delaware's Competition*, 117 HARV. L. REV. 588 (2003) (examining the federal government's encroachment into corporation law).

³⁰⁸ The other source of state laws across jurisdictions has been the National Conference of Commissioners on Uniform State Laws (NCCUSL) (also known as the Uniform Law Commission), which has sponsored drafts of more than 200 uniform laws on many different subjects, the most famous of which is the Uniform Commercial Code. They have not done a corporate law project since early in

largest corporations,³⁰⁹ and such other large commercial states as California and New York, follow their own statutory structure; yet, Delaware and the Model Act drafters have often appeared to have moved on similar paths. If the MBCA were to move on this topic, it seems likely that Delaware would be very willing to join in similar action. Delaware clearly has the most to lose from the current situation and would likely join a multistate effort to fix it. The harder question is why the legislatures of California or New York, or even Model Act states like Alabama or Arizona, would go along. Corporations headquartered in those states might well prefer to retain the safety valve of having the possibility of a suit brought in the courts of their state if that action (via a *Matsushita II* settlement) would help the corporation's lawyers achieve a more favorable settlement to class action litigation also being pursued in other jurisdictions.

While there are no mandatory requirements that states act in a coordinated fashion, there are a number of institutions in place that facilitate such action. Probably the best known group serving this role professionally over the years is the American Law Institute (ALI). Its past projects have addressed both principles of corporate governance and of aggregate litigation, but multijurisdictional representative litigation, a topic at the intersection of those two fields, was not included in either.³¹⁰ Moreover, such projects take years to reach completion and do not always succeed. While it is possible that the MBCA or the ALI could take action on this topic, it seems unlikely to us that the existing law reform organizations would be able to quickly and universally address the multijurisdictional litigation issues discussed in this paper.

6. *Private Ordering via Charter or Bylaw Provisions.*—Spurred by several practitioners³¹¹ and academics,³¹² private ordering forum selection provisions in corporate charters or bylaws have moved to the forefront in

the twentieth century. See Robert W. Hamilton, *Reflections of a Reporter*, 63 TEX. L. REV. 1455, 1457 (1985) (describing the promulgation of the Uniform Business Corporation Act by NCCUSL in 1928, its adoption in three states, and its withdrawal in 1958).

³⁰⁹ Marcel Kahan & Ehud Kamar, *The Myth of State Competition in Corporate Law*, 55 STAN. L. REV. 679, 698 (2002).

³¹⁰ In addition to traditional Restatements, and some model act projects, the ALI has also undertaken studies of areas of the law with more forward-looking suggestions. The first such project was the Principles of Corporate Governance in 1994. Such projects can become very controversial, as was the ALI's Principles of Corporate Governance project, and are therefore unable to command sufficient popular support to lead to reform.

³¹¹ For an important volume containing numerous articles by practicing lawyers on this topic, see M&A LITIGATION, *supra* note 76.

³¹² See, e.g., Joseph A. Grundfest, *The History and Evolution of Intra-Corporate Forum Selection Clauses: An Empirical Analysis*, 37 DEL. J. CORP. L. (forthcoming 2012) [hereinafter Grundfest, *History and Evolution*], available at <http://ssrn.com/abstract=2042758>; Joseph Grundfest, *Choice of Forum Provisions in Intra-Corporate Litigation: Mandatory and Elective Approaches* (2010) (unpublished manuscript) [hereinafter Grundfest, *Choice of Forum Provisions*], available at <http://ssrn.com/abstract=1690561>; see also Quinn, *supra* note 4 (detailing the use of the exclusive forum provision as a means to prevent litigation from leaving Delaware).

the recent debate over forum selection. The discussion was undoubtedly further stimulated by Vice Chancellor Laster's favorable remarks concerning these clauses in *In re Revlon*: "[I]f 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."³¹³

Some companies have put forum selection provisions in their charters prior to an initial public offering (IPO),³¹⁴ a few have submitted charter amendments to a shareholder vote,³¹⁵ but most of the adoptions by established public companies (still a small percentage of public companies) have been via director-passed bylaws,³¹⁶ likely reflecting concern that public company shareholders might vote against such proposed amendments if the question were put to them for decision.³¹⁷ As a result, some established public companies have been able to avoid seeking shareholder approval and instead inserted these provisions into their bylaws with only director approval.³¹⁸

These clauses typically allow the defendant corporation to designate the court in which shareholders of a defendant corporation can bring representative litigation.³¹⁹ Early forms of the clauses were more likely to be

³¹³ 990 A.2d 940, 960 (Del. Ch. 2010).

³¹⁴ Some corporations have adopted these provisions before their initial public offering to eliminate the need for shareholder approval. See CLAUDIA H. ALLEN, STUDY OF DELAWARE FORUM SELECTION IN CHARTERS AND BYLAWS ii (2011), available at http://www.ngelaw.com/files/Uploads/Documents/Exclusive_Forum_Provisions_Study_4_7_11.pdf (finding that charter amendments are being adopted by corporations "as they go public, emerge from bankruptcy protection or reincorporate in Delaware," thereby eliminating the necessity of shareholder approval); Grundfest, *History and Evolution*, *supra* note 312, at 23–25.

³¹⁵ During the 2011 proxy season, six public companies sought shareholder approval of forum selection charter amendments, and all but one passed; at least one additional proposal occurred in the 2012 proxy season. ALLEN, *supra* note 314, at 2.

³¹⁶ See *id.* at ii. Allen found that these companies made up 43.9% of companies with forum selection provisions. *Id.* Quinn argues that status quo bias is the reason for the infrequency of the adoption of these provisions. See Quinn, *supra* note 4, at 142.

³¹⁷ Institutional Shareholder Services' voting policies for the 2012 proxy season advised companies they would evaluate these "exclusive venue" provisions on a case-by-case basis, asking whether the company in question has good corporate governance structures currently in place and whether it has disclosed any material harm done to it by shareholder litigation in other jurisdictions. INSTITUTIONAL S'HOLDER SERVS., U.S. CORPORATE GOVERNANCE POLICY: 2012 UPDATES 13 (2011), available at http://www.issgovernance.com/files/ISS_2012US_Updates20111117.pdf.

Momentum to add a forum selection bylaw may also be impacted by litigation. See Bill Kelly & Elizabeth Weinstein, *Exclusive Forum Provisions Update*, DAVIS POLK BRIEFING: GOVERNANCE (June 21, 2012, 11:05 PM), www.davispolk.com/briefing/corporategovernance/?entry=186 (reporting lawsuits in Delaware courts against about a dozen companies for adding exclusive forum provisions via bylaws, of which two firms, Chevron and FedEx, continue to litigate the validity of the bylaws; this suggests most companies will wait for guidance from the chancery court before taking further action).

³¹⁸ ALLEN, *supra* note 314, at ii. While shareholders generally have the power to amend corporate bylaws, there have been no publicly disclosed attempts by shareholders to do so to date. *Id.*

³¹⁹ See Nathan, *supra* note 101, at 122 (providing an example of a forum selection clause).

mandatory in nature, requiring litigation to proceed in the state of incorporation, while more of the recent ones are elective clauses that give the corporation the option to require use of the state of incorporation or to permit litigation filed in the company's headquarters state to go forward.³²⁰

Proponents advance several arguments in favor of using charter or bylaw forum selection provisions: (1) they encourage consistent interpretation of the law of the state of incorporation, particularly in Delaware, and they may limit litigation of shareholder disputes to one forum, reducing duplicative law suit filings, while maintaining a convenient forum; (2) Delaware has a specialized court system with considerable expertise in corporate law that provides more certainty in outcomes; and (3) forum selection provisions in general are permissible as a matter of contract law, and the corporate charter is a contract. There are some problems with them as well: (1) a strong push by Delaware for such clauses may spark a backlash from other states, federal regulators, and plaintiffs' lawyers; (2) other states' courts may refuse to enforce them, leading to additional litigation in these representative actions claiming they impinge on shareholders' fundamental right to enforce the fiduciary duties that directors and officers owe them; and (3) as discussed below, the issue of shareholder consent, especially as to management-imposed bylaws.³²¹ On balance, while such provisions (if widely adopted and systematically enforced by foreign courts) may help reduce litigation agency costs, they may also increase managerial agency costs by giving corporate management control over one of shareholders' principal monitoring mechanisms to address managerial misconduct, making it difficult to know which approach maximizes social welfare.

Nor are we persuaded that the contract law analogy is conclusive. It is true that forum selection clauses are widely found in corporate contracts, such as merger agreements (as are a related set of clauses regarding choice of law).³²² And courts generally enforce them as a matter of contract law.³²³ In our setting, however, the contract is not between two corporations, but rather between the shareholders and managers within the corporation, raising the familiar issues of governance and shareholder monitoring of

³²⁰ Although the clear target of such clauses is representative litigation, in fact their language is broad enough to apply to direct actions by individual shareholders as well. See Grundfest, *Choice of Forum Provisions*, *supra* note 312, at 6–8 (showing two sample forum provisions).

³²¹ See Quinn, *supra* note 4, at 139–40; Faith Stevelman, *Regulatory Competition, Choice of Forum, and Delaware's Stake in Corporate Law*, 34 DEL. J. CORP. L. 57, 132–33 (2009).

³²² See Theodore Eisenberg & Geoffrey Miller, *Ex Ante Choices of Law and Forum: An Empirical Analysis of Corporate Merger Agreements*, 59 VAND. L. REV. 1975, 1982 (2006).

³²³ See, e.g., *Carnival Cruise Lines, Inc. v. Shute*, 499 U.S. 585, 593 (1991) (stating that a forum selection clause must be viewed under the realities of form passage contracts); *Bremen v. Zapata Off-Shore Co.*, 407 U.S. 1, 12–15 (1972) (holding that a venue provision in a freely negotiated contract should not be set aside absent a strong showing that enforcement would be unreasonable and unjust, or that the clause was invalid for such reasons as fraud or overreaching).

management agency costs.³²⁴ Corporate law permits contracting on such shareholder issues in some contexts, but not in others. After the *Smith v. Van Gorkom* decision, corporate statutes have permitted corporations to include provisions in their articles of incorporation by which they may exculpate directors for breaches of the duty of care, but not the duty of loyalty.³²⁵ These charter amendments must be approved by shareholders.³²⁶ In other areas, such as dual class recapitalizations, even shareholder-approved charter amendments have been prohibited because their potential effect of increasing managerial agency costs is too great. Are forum selection provisions permissible given their potential impact on shareholders' ability to bring suit to limit managerial agency costs?

Should shareholders be bound when directors use their broad powers in corporate law to insert such a provision into the bylaws without a direct shareholder vote? At present, there appears to be little support for allowing these bylaws. For example, when Vice Chancellor Laster raised the visibility of this issue, he expressly referred to action by both "directors and stockholders" that they believe it would be value enhancing,³²⁷ highlighting the importance of shareholder approval of forum selection provisions. Furthermore, opponents of director bylaw provisions won the first case raising this issue when, in *Galaviz v. Berg*, a federal district court rejected a forum selection provision in the bylaws of Oracle corporations that required all derivative actions to be filed in the Court of Chancery in Delaware.³²⁸ Based on this bylaw, the defendants moved to dismiss the case on the basis of wrongful venue, claiming that the bylaw constituted an enforceable provision under contract law.³²⁹ That the bylaw had been unilaterally adopted by the directors after plaintiff shareholder brought a derivative action claiming that the board had breached their fiduciary duties eliminated the consent needed to support a contract analogy.³³⁰

³²⁴ See *supra* Part I.A.

³²⁵ See DEL. CODE ANN. tit. 8, § 102(b)(7) (2011).

³²⁶ *Id.* § 242(b)(2) (2011) (requiring approval of shareholders for amendment of articles).

³²⁷ *In re Revlon, Inc. S'holders Litig.*, 990 A.2d 940, 960 (Del. Ch. 2010); see ALLEN, *supra* note 314, at iv (92.7% of forum selection clauses adopted after Laster's statement).

³²⁸ See 763 F. Supp. 2d 1170, 1174 (N.D. Cal. 2011) ("[T]he venue provision was unilaterally adopted by the directors who are defendants in this action, after the majority of the purported wrongdoing is alleged to have occurred, and without the consent of existing shareholders who acquired their shares when no such bylaw was in effect.").

³²⁹ *Id.* at 1171.

³³⁰ *Id.* at 1174–75. The court did note that if the corporation had obtained such consent, then its contract law arguments would be stronger. There is a split of the federal circuits as to whether this question should be determined by state law or federal common law. Compare *Manetti-Farrow, Inc. v. Gucci Am., Inc.*, 858 F.2d 509, 513 (9th Cir. 1988) (federal common law applies to the enforceability of the venue provision because the federal procedural interests "significantly outweigh the state interests" under *Erie*), with *Gen. Eng'g Corp. v. Martin Marietta Alumina, Inc.*, 783 F.2d 352, 356–57 (3d Cir. 1986) (forum selection clause was a contract question and should generally be a state law matter, except when there is a significant conflict between some federal policy or interest and the use of state law); see also *Nutter v. New Rents, Inc.*, No. 90-2493, 1991 U.S. App. LEXIS 22952, at *14–20 (4th Cir. Oct. 1,

A separate issue is whether jurisdictional or constitutional issues prevent a forum selection clause. Citizens are able to use the general jurisdiction of the various states to sue defendants over whom that court has personal jurisdiction, and individual states are unable to divest another state from asserting such jurisdiction.³³¹ Federal law provides a litigant the ability to pursue a state law claim in a federal tribunal if the plaintiff wants to avoid the home-state courts of the defendant; forum selection clauses seek to prevent plaintiffs from making such choices.³³² Interestingly, the court often chosen by plaintiffs is not a federal court but rather a state court in the state of the corporation's headquarters.³³³ Such a court, if anything, would be sympathetic to the interests of the hometown corporation and less interested in a shareholder representative from out of state. Such a pattern illustrates that the reality is that forum selection behavior is more about attorneys' fees (and more particularly which sets of attorneys gets fees), and neither diversity jurisdiction nor general jurisdiction has much to say. Apart from corporate law, the balance ought also to take into account the procedural values of letting parties bring suit against defendants in jurisdictions where they can be reached and permitting parties to have access to federal courts as a response to possible home court discrimination.³³⁴

1991) (forum selection clause was a matter of state law); *Snider v. Lone Star Art Trading Co.*, 672 F. Supp. 977, 982 (E.D. Mich. 1987) (finding state law governs the forum selection clause), *aff'd*, 838 F.2d 1215 (6th Cir. 1988).

³³¹ *Tenn. Coal, Iron & R.R. v. George*, 233 U.S. 354, 359 (1914) (holding that a state cannot, by legislation, effectively divest another state's courts of the power to hear cases over which they would otherwise have jurisdiction).

³³² *See* U.S. CONST. art. III, § 2 (granting judiciary the authority to hear diversity cases); 28 U.S.C. § 1332 (2006) (providing for diversity jurisdiction); *see also* Stevelman, *supra* note 321, at 131 (“[A]ny measures to limit shareholder-plaintiffs’ otherwise legitimate access to the federal courts would almost certainly prove unconstitutional.”).

³³³ *See* Cain & Davidoff, *supra* note 36, at 13 n.7.

³³⁴ Delaware has asserted a countervailing constitutional interest in having its substantive law apply under the internal affairs doctrine. *See* *McDermott Inc. v. Lewis*, 531 A.2d 206, 217 (Del. 1987) (application of the internal affairs doctrine mandated by constitutional principles, except in the rarest situations). Its courts have also asserted constitutional support for the broad reach of its courts’ jurisdiction in deciding internal affairs disputes. *Armstrong v. Pomerance*, 423 A.2d 174, 177 (Del. 1980) (“If it be conceded, as surely it must, that Delaware has the power to establish the rights and responsibilities of those who manage its domestic corporations, it seems inconceivable that the Delaware Courts cannot seek to enforce these obligations but must, rather, leave the lion’s share of the enforcement task to a host of other jurisdictions with little familiarity or experience with our law, jurisdictions which may or may not even choose to apply Delaware law depending on the vagaries of each jurisdiction’s choice of law rules. We find nothing in ‘traditional notions of fair play and substantial justice’ which compels such anomalous results.”). In the recent debate over multiple filings, the argument has extended to Delaware’s primacy as a forum, not just the source of substantive law, albeit an argument based on comity and public policy rather than constitutional requirements. *In re Topps Co. S’holders Litig.*, 924 A.2d 951, 961 (Del. Ch. 2007) (“Representative plaintiffs seeking to wield the cudgel for all stockholders of a Delaware corporation have no legitimate interest in obtaining a ruling from a non-Delaware court.”). *See* Part II.C.2 for a discussion of comity.

Weighing these arguments, we are not persuaded that charter and bylaw provisions are the best solution to the issues raised by fee distribution litigation for several reasons. First, as we discussed in Part II.B.3 above, it is important to remember that forum selection clauses are nothing more than forum shopping by defendants. There is little reason to privilege defendant forum shopping over plaintiff forum shopping. Second, the use of bylaws that can be implemented without shareholder consent, or even charter amendments that require such consent, forces us to confront the weakness of shareholders' voting rights under current law. Starting with bylaws—the weaker of the two provisions—proponents of these amendments have argued that in most situations shareholders have the power to amend bylaws imposed by incumbent boards of directors and that this is sufficient protection against self-interested director conduct.³³⁵ Given the substantial collective action problems shareholders would face in launching a ballot initiative to change a bylaw, particularly one that does not involve a change-of-control transaction, and the fact that management could then quickly reverse the shareholders' action in most states, investors will not be able to change bylaw provisions except when faced with the most egregious wrongdoing. Effectively, this would make bylaw changes virtually irreversible unilateral director action absent the kind of unusual shareholder activism seen in classified board provisions.³³⁶

The case for charter amendments is stronger, but still fraught with difficulty. On the plus side, charter amendments require a shareholder vote,³³⁷ which provides some protection to investors, although they still face collective action problems. The presence of third-party voting advisors that issue voting recommendations on forum selection clause votes should help to overcome the collective action problem in this situation.³³⁸ Nevertheless, as Professor Gordon has aptly noted in his work on dual class recapitalizations, shareholder approval of charter amendments does not necessarily lead to the conclusion that they increase shareholder wealth. In fact, these amendments may actually decrease wealth.³³⁹ He argues that the

³³⁵ This is a particularly suspect claim where directors are adopting such amendments after they have been sued for alleged misconduct, or where they adopt bylaws that give the board the discretion to select one forum among a group of potential forums once shareholder litigation has been filed.

³³⁶ For classified boards, shareholders have had to make precatory Rule 14a-8 shareholder proposals seeking a vote on the removal of the classified board, obtain a majority vote of the company's shareholders in favor of such action, and then persuade the company's board of directors to allow shareholders to vote to remove the classified board from the company's certificate of incorporation. Thomas & Cotter, *supra* note 24, at 370, 377–78, 384, 389. Such activism has become more common in recent years. *See id.* at 388–89.

³³⁷ *See, e.g.*, DEL. CODE ANN., tit. 8, § 242(b) (2011).

³³⁸ ISS has issued voting guidelines to its clients concerning forum selection clauses. *See INSTITUTIONAL S'HOLDER SERVS.*, *supra* note 317, at 13.

³³⁹ Jeffrey N. Gordon, *Ties that Bind: Dual Class Common Stock and the Problem of Shareholder Choice*, 76 CALIF. L. REV. 1, 23 (1988).

presence of collective action problems³⁴⁰ and strategic choice issues³⁴¹ undercut efficiency-based arguments for charter amendments in that setting.

Similar arguments may be made against forum selection clauses, as they can have a management-protection purpose that motivates them as well. For example, while we do not yet know the shareholder profile of firms that have proposed, or will propose, forum selection amendments, it is possible that they may be skewed toward firms with high insider stock ownership and low levels of institutional shareholdings. Management might also use sweeteners, or implicit threats, to induce shareholders to approve these charter amendments. We hasten to add that it is currently too soon to tell if these things will occur, but they are significant potential problems that could be manifested in shareholder votes on forum selection charter amendments.

Finally, we worry about the lock-in effect of such provisions. As we noted with bylaws, it will be very difficult for shareholders to organize to remove a bylaw, and it is effectively impossible for them to remove a charter amendment without board cooperation because directors alone have the power to recommend such changes. Almost all of these forum selection provisions are aimed at forcing plaintiffs to file representative litigation in Delaware.³⁴² What will happen to shareholders' power to sue if the Delaware courts were to manifest extreme hostility to these cases? At present, Delaware seems, in most cases, to be doing an excellent job balancing investor and management interests, but there are many who doubt this claim both today and historically.³⁴³ We think that this requires careful consideration before any rush to permit corporate forum selection provisions.

CONCLUSION

One of the key problems that American corporate law has struggled with for the past eighty years is how to constrain managerial conduct when

³⁴⁰ The evidence summarized in the article shows that firms making such proposals tend to have lower than average institutional ownership and greater insider stock ownership. *See id.* at 45.

³⁴¹ In that context, Gordon claims that management may tie the recapitalization to an unrelated dividend sweetener or threaten to take action adverse to shareholder interests if their proposal is defeated. *See id.* at 47.

³⁴² *See ALLEN, supra* note 314, at i.

³⁴³ The race to the top versus race to the bottom debate over the impact of Delaware law on shareholder welfare has been going on for generations. For a good summary of the literature favoring the race to the top viewpoint, see ROMANO, *supra* note 82. In recent years, Lucian Bebchuk has been the strongest advocate for the race to the bottom perspective. *See, e.g., Lucian Arye Bebchuk, Federalism and the Corporation: The Desirable Limits on State Competition in Corporate Law*, 105 HARV. L. REV. 1435 (1992). Mark Roe has recently argued that the federal government is the party that most actively influences state corporate law. *See, e.g., Mark J. Roe, Delaware's Politics*, 118 HARV. L. REV. 2491 (2005).

ownership is separated from control.³⁴⁴ Our corporate law relies heavily on the limited shareholder powers of voting, selling, and suing to help in that effort. Derivative suits and class actions remain core instruments used to check the broad control that corporate law gives directors and managers over the collective assets owned by others. Not only are these litigation rights longstanding, but they are split between two levels of government—both as to substance and as to procedural rules—which ensures that multiple routes are possible in many corporate disputes. This leads to the possibility of strategic behavior by plaintiffs in filing one cause of action versus another.

From our focus on the intended governance role of litigation—the deliberate choice in our polity to provide dueling sources of law to provide the basis for such litigation and the economic reality that follows from giving law firms center stage in providing this enforcement—we develop a theory of shareholder litigation as applied to contemporary corporate and securities law. In our theory, the outcome of this effort to constrain management agency costs without generating excessive litigation agency costs necessarily must model not just the legal rules, but also the roles of plaintiff law firms, defendant law firms, and courts. There are times that the interaction of these three groups will produce a beneficial combination, and times when it may not. In short, shareholder litigation experiences a dynamic process over time that requires constant balancing of managerial agency costs and litigation agency costs.

Shareholder suits filed in multiple jurisdictions raise many of the same issues of class actions generally. In addition, any effort to address them must take into account the distinctive role of shareholder litigation in corporate governance. However, like other class actions, the economics of shareholder litigation mean that attorneys have the prime economic incentive to pursue these suits and attorney self-interest can distort the process. Such litigation agency costs are regularly weighed against litigation's role in combating undue losses from management agency costs. Multiple-plaintiff law firms seeking to represent the group—and to share in attorneys' fees that may follow from such suits—are one cause for the proliferation of suits within a single jurisdiction. This interacts with the incentives of different law firms to pursue jurisdictions other than the place of incorporation if that produces a better result (which can be measured in terms of greater recovery for the class, or rearranging the distribution of attorneys' fees or extracting rents from the process).

Applying our theory to the multijurisdictional representative shareholder litigation that is observed today, we see again the importance of balancing managerial agency costs and litigation agency costs. On the managerial agency cost side of the ledger, permitting shareholders (and

³⁴⁴ ADOLPH A. BERLE & GARDINER C. MEANS, *THE MODERN CORPORATION AND PRIVATE PROPERTY* 119 (rev. ed. 1968).

courts) to determine where it is appropriate to file their representative actions has value because it reinforces the importance of that limited power. Furthermore, keeping an open market for corporate law so that the Delaware courts do not establish a virtual monopoly on litigation issues gives that state's courts a continuing incentive to listen to shareholder concerns.

On the cost side, it is not clear that multijurisdictional litigation creates significant costs. The additional filing of derivative suits as tagalongs to Rule 10b-5 lawsuits is likely more of a rearranging of the pool of attorneys' fees; it likely does not affect the size of that pool or even the size of the recovery, and may add some corporate governance benefits when those cases settle. For mergers and acquisitions class action litigation in state courts, the fact that should be of greatest interest to legal reformers is not the percentage of deals that attract suits (particularly in the post-financial-crisis period when the number of deals decreased markedly), but the number of deals in which lawyers receive fees separate from recovery for shareholders and the size of those fees. There is not at this time sufficient empirical evidence that the number of deals experiencing litigation has increased significantly, nor that the cost of settling a strong set of cases varies much depending on whether they are filed in one jurisdiction or another. For traditional derivative suits in state courts, the existing empirical evidence is too weak for us to draw firm conclusions.

Given the limited costs and benefits associated with multijurisdictional shareholder litigation, we believe that a low-cost, easily implemented solution that can be readily reversed is the best answer. We believe that judicial comity is the best, lowest cost option currently available. We consider, but reject, forum selection bylaws and charter provisions because they are effectively irreversible, provide inadequate protection of shareholder interests, and constitute defendant forum shopping. However, in reaching these conclusions, we recognize that they are based on the current empirical evidence concerning these suits. As our theory points out, times change, and the balance between litigation agency costs and managerial agency costs must be reassessed as they do.

