CUG.COMments

A Newsletter from Chicago Underwriting Group, Inc.
Underwriters of D & O and Professional Liability Insurance

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In this issue…we follow up on some items from earlier newsletters.

1. Exclusive-Forum Provisions

When the topic of exclusive-forum provisions was first discussed in the May 2012 newsletter, the push by public companies to control the venue for certain types of shareholder litigation had stalled. With more than a dozen companies facing shareholder lawsuits, all but two of the corporate defendants had decided to withdraw their planned exclusive-forum bylaw amendments.

The principal benefit of such an amendment is that it helps mitigate the considerable cost and aggravation of defending duplicate shareholder lawsuits filed in different states. For their part, shareholder activists and some shareholder advocates were opposed to the idea that they might be prevented from filing a lawsuit in a forum of their choice.

Those remaining two companies, Chevron Corporation and FedEx Corporation, elected to have their cases heard in court – the Chancery Court of the State of Delaware.

The Court Decides

Being for practical purposes similar grievances, the two cases had been combined for the hearing. On June 25, 2013, the court's decision was handed down. In a 47-page decision, Chancellor Leo Strine concluded that the forum selection clauses "are contractually valid and enforceable," a significant victory for the corporate defendants and a green light —albeit qualified— for other Delaware-incorporated companies to proceed with similar bylaw amendments.

Comment

The decision can be appealed to the Delaware Supreme Court, and so a final disposition for Delaware companies may have to wait. The reaction of state courts outside Delaware also remains to be seen. If it holds up on appeal, the opinion rendered by Chancellor Strine will be law in Delaware, and should be deferred to by other jurisdictions when facing actions involving Delaware companies, but a shareholder challenge to a company incorporated in a different state may yet produce a different result.

Chancellor Strine pointed out that shareholders still have some remedies: a majority can push for new bylaws, or lawsuits may be filed for possible inequitable conduct if the situation merits.

It would have been a surprise had the Chancellor decided differently. The Delaware Chancery Court is proud of its status as the primary arbiter of the nation's corporate disputes, being the state of choice for the vast majority of incorporations. To quote from its web site:

> "The Delaware Court of Chancery is widely recognized as the nation's preeminent forum for the determination of disputes involving the internal affairs of the thousands upon thousands of Delaware corporations and other business entities through which a vast amount of the world's commercial affairs is conducted. Its unique competence in and exposure to issues of business law are unmatched."

The reality behind a forum selection provision for a Delaware company is that the company will almost certainly select Delaware as its preferred forum, a state acknowledged to be generally sympathetic to businesses. That being so, a decision from the Chancery Court repudiating a Delaware company's right to select a forum would be tantamount to inviting plaintiff shareholders to litigate outside the state. That would seem at odds with the Delaware Chancery Court's self-declared role.

2. The Neal Bill (CUG.COMments January 2011)

With a dogged persistence that might be described as Sisyphean, Representative Richard Neal of Massachusetts recently reintroduced his bill to defer or deny the tax deduction for premiums paid by an insurance company to its foreign affiliates, if the premiums are not subject to U.S. tax. This is the fourth attempt by Rep. Neal to pass his measure into law, following unsuccessful efforts in 2008, 2009, and 2011. The underlying intent is two-fold: first to capture lost federal tax revenues (estimated in 2011 at around $12 billion over ten years), and second, to level the playing field for U.S. insurers not able to utilize that tax deduction.

The chief proponents and opponents shuffled (once again) into position to declare their interest. The Coalition for a Domestic Insurance Industry "affirmed its strong support," and urged Congress to "swiftly adopt the proposed legislation." For its part, the Coalition for Competitive Insurance Rates "strongly objected."

Comment

There is on the surface little to distinguish this latest initiative from that of 2011, in either the provisions of the bill or the rhetoric of the opposing factions. Also unchanged is the hope —or fear— that the key features of the bill may be quietly included within a more expansive fiscal measure.

What has changed, however, is the progressive strengthening of the global reinsurance market. According to a report by Aon Benfield, reinsurer capital shrank by around 3% from 2010 to 2011. But reinsurer capital increased by 11% during 2011, and by a further 2% between January, 2012 and March, 2013. "Supply," states the report, "remains abundant in all global regions." This robustness could undermine a key tenet of the anti-Neal bill lobby, that the measure would "drastically decrease insurance capacity in this country."

3. Dodd-Frank Whistleblower Update

Since news of the first whistleblower award was reported in the CUG.COMments issue of January 2013, there has been only one more award. Actual payment is contingent upon the amount collected from the perpetrators by the Securities and Exchange Commission (SEC), but so far the SEC has not recovered anything. All is not lost, as the Department of Justice has managed to collect $800,000, and whistleblowers will be able to apply for an award based on that amount. But with just two awards (and only one payment) since the program's introduction in 2011, the much-vaunted incentive for insiders to reveal corporate wrongdoing threatens to fade into irrelevance. For it to succeed, the program probably needs a highly visible case that results in a massive fine for the wrongdoer and a substantial award to the whistleblower. ❖

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Chicago Underwriting Group, Inc.

Web: www.cug.com
Email: info@cug.com
Phone: (312) 750-8800
Fax: (312) 750-8965

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