

The Delaware Court of Chancery Defers to the State of Incorporation in Matters of a Company's Internal Affairs

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Sylebra Cap. Partners Master Fund, Ltd., et al. v. Perelman, et al., C.A. No. 2019-0843-JRS (Del. Ch. Oct. 9, 2020), Sights, V.C.—
The Delaware Court of Chancery dismissed a plaintiff shareholder's request for declaratory and injunctive relief related to the defendants' purported denial of certain property rights based on the internal affairs doctrine and a forum selection bylaw. The decision reflects the court's refusal to examine the governance of a foreign entity for which such matters are better decided by the state of incorporation.

Here, the plaintiff shareholder filed suit against Scientific Games Corporation (SGC), SGC's controlling shareholder, and its board of directors related to acts undertaken by the defendants which impaired the plaintiff's ability to redeem its shares for fair value. The plaintiff alleged that SGC, which was previously incorporated under the laws of the state of Delaware but is now a Nevada corporation as a result of a reincorporation merger, adopted and enforced suitability requirements against it as part of its controlling shareholder's campaign to drive the plaintiff from the company and consolidate its power. SGC's former charter set forth the suitability requirements, which the company relied on when notifying government regulators of the plaintiff's purported misconduct. During the regulators' investigation, SGC amended its bylaws to allow the company to invalidate shares under certain conditions and to require the company to conduct a suitability analysis of each significant shareholder. Several months later, SGC announced plans for a merger to reincorporate under Nevada law. The company distributed proxy materials, and the merger was approved. SGC adopted a new charter and bylaws, which expanded its investigative power. The company directed its powers at the plaintiff, and the plaintiff's refusal to comply led to the filing of a lawsuit by SGC against the plaintiff in Nevada state court. After the plaintiff failed to remove the action to federal court, it filed suit in the Court of Chancery.

In *Sylebra*, the court granted the defendants' motion to dismiss based on a forum selection clause in SGC's bylaws. As expected, the court adhered to the internal affairs doctrine, and thus deferred to the authority of the state of incorporation over the internal affairs of the company. Although SGC was once incorporated under the laws of the state of Delaware, it reincorporated in Nevada and the plaintiff failed to enjoin the reincorporation merger to avail itself of the Delaware courts.

The court also gave effect to a forum selection bylaw, which required the plaintiff to bring suit in Nevada. A forum selection bylaw carries a presumption of validity. In order to escape its legal effect, the plaintiff must clearly show that enforcement is unreasonable, unjust, or unlawful. The plaintiff failed to carry its burden in *Sylebra*. First, it argued that it did not consent to the bylaw, because it was unable to sell its shares at the time of the bylaw's adoption. The argument implies a freedom to sell shares, which lacked a basis of support not only in SGC's charter, but also in Delaware law. Second, the plaintiff argued that the forum selection bylaw was unreasonable because it was adopted after the defendant directors' alleged wrongdoing. A shareholder agrees to be bound by current and future bylaws when it purchases shares in a company, and the timing of alleged wrongdoing relative to the adoption of a forum selection bylaw is irrelevant. The court also found that the plaintiff failed to allege any facts which question the integrity of the Nevada courts to resolve the dispute. Third, the plaintiff argued that the forum selection bylaw was the product of fraud, but the complaint was devoid of any allegations of fraudulent conduct. Accordingly, the court dismissed the complaint.

Sylebra reinforces the commitment of the Court of Chancery to the internal affairs doctrine. The case also serves as a reminder for parties to act in a timely manner. Had the plaintiff sought to enjoin the reincorporation merger, it could have asserted its claims in Delaware state court. While the merits of those claims are in dispute, the plaintiff's delay permitted the reincorporation merger to occur and limited the forum to Nevada state court.