**recent DEVELOPMENTS in**

**OKLAHOMA business and corporate law ‑ 2014**

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**Introduction**

The economic recession and the Federal regulatory response have dominated this topic since 2007. We have talked about the mortgage crisis, the derivatives markets, the collapse of global financial institutions, an unsettling, world-wide economic downturn, Federal bailouts and sweeping regulatory changes. And the dominance is deserved. The pace of change in this area of law races to catch markets and industries that come and go and morph in unexpected ways.[[1]](#footnote-1) The combination of technological advances, increased information flows, greater productivity, and globalized expansion have produced a rate of global economic change not witnessed since the Industrial Revolution.[[2]](#footnote-2) One could argue that the rapid pace of change within the financial markets – and the inability of investors and regulators to fully understand the changes – was a principal cause of the financial collapse and resulting recession.[[3]](#footnote-3)

In some ways, the law still struggles to keep up. Significant parts of the massive Dodd-Frank Act – passed in 2010 in the wake of the financial collapse – were implemented only recently or have yet to be implemented.[[4]](#footnote-4) The JOBS Act passed in 2012 and was designed to improve capital access for private companies. While the number of initial public offerings has finally rebounded in the U.S., and many companies are using the expedited procedures provided under the JOBS Act, other aspects of the JOBS Act – notably the crowdfunding rules – are proposed, but not yet adopted.[[5]](#footnote-5) The delays in implementation are often due to the complexity of the matters to be regulated.

Other developments reflect these complexities and our struggle to find a proper relationship with business entities. This is evident in the trends in criminal prosecution of business entities.[[6]](#footnote-6) Historically, if a corporation were accused of wrongdoing, the responsible individuals might be prosecuted. The corporation itself would be sued civilly. That is changing. The criminal prosecutions of corporations and the amount of recoveries are both increasing dramatically. This year will break all records. American financial institutions have already paid over $50 billion year-to-date to settle criminal charges related to mortgage-backed bonds and other financial misconduct. Foreign financial institutions have paid billions more in settlement of criminal charges.[[7]](#footnote-7) The criminal charges extend beyond financial institutions. BP paid $13 billion to settle criminal charges for the Deepwater Horizon oil spill. Toyota, the world’s largest automaker, paid $1.2 billion to settle criminal charges relating to its cars.[[8]](#footnote-8) Wal-Mart, the world’s largest retailer, and General Motors, the largest U.S. automaker, are reportedly discussing the settlement of criminal charges.[[9]](#footnote-9)

This is not to say that some misconduct does not warrant criminal charges. But criminal charges can be brought under a myriad of regulations by Federal or state regulators.[[10]](#footnote-10) Settlement proceeds may go to the prosecuting agency and often never reach the victims of the misconduct.[[11]](#footnote-11) The prosecuting agency’s retention of settlement proceeds create powerful financial incentives for aggressive prosecution and can lead to over-enforcement.[[12]](#footnote-12) A corporation may be prosecuted in one jurisdiction, but not others, resulting in distributions of proceeds unrelated to the harm done.[[13]](#footnote-13) The settlements are typically confidential, which means a lack of transparency in the process. The public does not necessarily know the underlying facts or the prosecutor’s justification for the settlement amount. Without a full understanding of the misconduct and a measure of the settlement, there are no guideposts by which other businesses might improve their compliance practices, which weakens the deterrent effect of the criminal charges.[[14]](#footnote-14)

The growth in criminal prosecutions of businesses has resulted in an environment that often seems unpredictable, arbitrary, and inequitable. Corporations can pay very large settlements, which ultimately cost the shareholders and innocent employees, while culpable individuals within the corporation are not punished. Federal Judge Jed Rakoff has argued that the “failure of the government to bring to justice those [individuals] responsible for [the wrongdoing] bespeaks weaknesses in our prosecutorial system that needs to be addressed.”[[15]](#footnote-15) Other commentators have argued for better transparency and consistency in the settlements.[[16]](#footnote-16) Understanding the facts of the case and how the law is applied is important in an open society operating under the rule of law.

Another example of our complicated relationship with legal entities is the recent Supreme Court case of *Burwell v. Hobby Lobby Stores, Inc*.[[17]](#footnote-17) The facts in the case were well publicized, if not politicized. Three closely held corporations sued the Federal Department of Health and Human Services to avoid providing certain contraceptive drugs and devices under their employee health insurance plans, as required under the Affordable Care Act (the “*ACA*”).[[18]](#footnote-18) They contended that providing the drugs and devices substantially burdened their free exercise of religion, which was protected under the Religious Freedom Restoration Act (the “*RFRA*”).[[19]](#footnote-19) The Tenth Circuit had affirmed the claims of Hobby Lobby and Mardel, companies owned and operated by the Green family.[[20]](#footnote-20) The Third Circuit had denied the claims of Conestoga Wood Specialties, which was owned and operated by the Hahn family.[[21]](#footnote-21)

The central issue in *Hobby Lobby* was whether a for-profit corporation could claim the protections of the RFRA and thus avoid the contraception mandates of the ACA. Within this central issue were many sub-issues involving the scope of the ACA and the RFRA, free speech and other constitutional law questions, statutory construction and Congressional intent, which are beyond the scope of this paper.

For corporate law purposes, the case raises fundamental issues about the nature of legal entities and their relationship to their owners. Can a for-profit corporation have religious beliefs? Can the religious beliefs of the owners be imputed to the corporation? Does that imputation void the legal separation between the corporation and its owners?

Justice Ginsburg in dissent took the historical position. She quoted Chief Justice John Marshall, who wrote in 1819, “[A corporation is] an artificial being, invisible, intangible, and existing only in contemplation of law.”[[22]](#footnote-22) She then turned to Justice John Paul Stevens, who wrote more recently, “[Corporations] have no consciences, no beliefs, no feelings, no thoughts, no desires.”[[23]](#footnote-23) Justice Ginsburg argued that the primary purpose of a for-profit corporation is to make money. Any charitable or religious expression was merely incidental to the corporation’s primary purpose. While no one would doubt the sincerity of the owners’ religious beliefs, imputing those beliefs to the corporation ignored the legal separation between the corporation and its owners.

Justice Alito in the majority argued that a for-profit corporation can legally “exercise a religion” since a corporation is not limited in its purposes. For-profit corporations often engage in charitable activity. He further argued that the act of incorporation should not deprive an individual of his or her religious beliefs. For him, a closely held, family owned and operated corporation can reflect the religious beliefs of its owners. He would not draw a bright line between the corporation and its owners.[[24]](#footnote-24)

While these issues composed only portions of Justice Alito’s and Justice Ginsburg’s respective opinions, they were heavily briefed. An *amicus* brief was filed by 44 corporate and criminal law professors, which argued that a corporation is a distinct legal entity separate from the beliefs of its shareholders.[[25]](#footnote-25) It argued that this distinction is “essential” to “the orderly conduct of business” and that “there is no basis . . . to disregard the separateness” in the *Hobby Lobby* case.[[26]](#footnote-26) It argued that Hobby Lobby was attempting to “reverse veil pierce” by imputing the shareholders’ beliefs to the corporations and that application of the concept was inappropriate.[[27]](#footnote-27)

While neither Justice used the term “reverse veil pierce” (“*RVP*”), the concept was evident in the opinions. Another corporate law professor, Stephen Bainbridge, had suggested that RVP could be an appropriate position for Hobby Lobby to take.[[28]](#footnote-28) Bainbridge argued that RVP permits a court to disregard a corporation’s separateness to allow shareholders to enjoy benefits otherwise available only to individuals. He further argued that RVP should apply to shareholders seeking protection under the free exercise clause of the First Amendment or the RFRA. The *amicus* brief took issue with Bainbridge’s position, to which Bainbridge replied in another essay published before the *Hobby Lobby* opinion was released.[[29]](#footnote-29)

*Hobby Lobby* may be important not for answers it gives, but for the questions it raises. We now know that Hobby Lobby, Mardel and Conestogo are exempt from certain conceptive requirements of the APA. But who else is exempt? Who are “closely held corporations”?[[30]](#footnote-30) Which closely held corporations have religious beliefs? What happens if some, but not all, shareholders agree? What unexpected consequences might flow from disregarding the legal separation? Will the RFRA protect corporations from other regulatory burdens? These questions show that our understanding of and relationship with legal entities is far from certain. Seeking the truth is indeed an ongoing task.

### Oklahoma Developments

National events may have diverted attention from, but have not diminished, state level activity. The Legislature passed Senate Bill 1799, which applies a prevailing party rule for payment of attorney fees in shareholder derivative actions. The Legislature did not pass two other bills. One would have updated the Oklahoma General Corporation Act and the Oklahoma LLC Act. Another would have adopted the Revised Uniform Unincorporated Nonprofit Association Act. We also have recent Oklahoma cases touching on corporate law.

#### Legislation

*Senate Bill 1799*. The Legislature passed one bill in 2014 dealing with business entities, which was Senate Bill 1799. The bill amended the Oklahoma General Corporation Act’s section dealing with shareholder derivative actions.[[31]](#footnote-31) It added a subsection providing that a court may award attorney fees to a plaintiff if the compromise or settlement of the derivative action confers a substantial benefit upon the corporation. This generally restates existing law.[[32]](#footnote-32) It added another subsection requiring the non-prevailing party to pay the attorney fees of the prevailing party in derivative actions. This subsection departs from existing law.

To understand the bill, one must examine the rapid growth in derivative actions against announced merger and acquisition transactions.[[33]](#footnote-33) Researchers Daines and Koumrian found that in 2007 approximately 53% of M&A transactions over $500 million were challenged in court. In 2012, 96% of those transactions were challenged. Virtually all of those cases were usually settled within weeks of filing to permit the transaction to close. Over 80% were settled with only changes in the disclosure documents and, in 98% of the settlements, the shareholders received no increase in the merger price or other compensation. The corporations paid on average $725,000 per settlement to the plaintiff lawyers in addition to paying for their own defense.[[34]](#footnote-34)

The rapid growth in these “disclosure only” settlements has been described as a tax upon M&A transactions and inimical to the shareholders’ best interests since the shareholders receive no financial benefit and bear all of the litigation costs.[[35]](#footnote-35) The settlements have drawn some criticism from courts in Delaware and Texas.[[36]](#footnote-36)

Corporations have responded by adopting forum selection bylaws, which require shareholder suits to be filed in a designated jurisdiction. These bylaws consolidate the litigation in a single forum and avoid the cost of multi-district litigation. They also avoid forum shopping for jurisdictions perceived to be more favorable to the plaintiff claims.[[37]](#footnote-37) Since most of public corporations are domesticated in Delaware, the chosen forum is usually Delaware. The Delaware courts are seen as a more predictable forum, which reduces the risks of outlier rulings. Several courts have affirmed the enforceability of these bylaws and confidence has grown in their use.[[38]](#footnote-38)

More recently, corporations have begun adopting prevailing party bylaws, which require a plaintiff to pay the corporation’s legal fees if it does not obtain a judgment on the merits that substantially achieves the full remedy sought. The adoption of prevailing party bylaws gained momentum when the Delaware Chancery Court affirmed such a bylaw in [*ATP Tour, Inc. v. Deutscher Tennis Bund*](http://courts.state.de.us/opinions/download.aspx?ID=205490).[[39]](#footnote-39) This case involved a non-profit corporation, but the rational would seem to apply to for-profit corporations as well.

Soon after the *ATP Tour* decision, the Delaware bar committee caused legislation to be introduced that would prohibit prevailing party bylaws, fearing that their use would tip the scales too far and discourage meritorious derivative actions.[[40]](#footnote-40) While the bar committee’s legislative recommendations are usually followed in Delaware, the U.S. Chamber and other business interests lobbied against the bill and the Delaware Governor and legislature deferred action pending further study of the matter.[[41]](#footnote-41)

The Oklahoma legislature did not wait. At least one Oklahoma corporation had experienced a disclosure only settlement and others feared they might.[[42]](#footnote-42) They pushed for passage of SB 1799, which was adopted and became effective November 1, 2014. The prevailing party statute applies to all derivative actions, whether settled or adjudicated, and is mandatory.[[43]](#footnote-43) The statute will most certainly discourage the filing of derivative actions for disclosure only and other non-monetary settlements. Plaintiffs must risk payment of the corporation’s legal fees for no possibility of monetary gain. How the prevailing party statute will affect more meritorious derivative actions remains to be seen. One might surmise that small shareholders in large corporations would not file an action regardless of its merits when their share of any award is small and their risk of loss is large. While the upsurge in derivative actions is a phenomenon affecting public corporations, the prevailing party statute applies to closely held corporations as well. Shareholders in closely held corporations may have relatively larger ownership interests than the typical shareholders in public corporations. Yet even a larger shareholder might pause before facing all litigation costs. If we find the statute is discouraging meritorious claims as well as the frivolous, further amendments will be necessary. As adopted, SB 1799 applies only to corporations and does not affect LLCs or partnerships.

*House Bills 1995 and 1996 ‑ General*. Two bills covering legal entities were carried over from the 2013 session and failed to pass in the 2014 session. House Bill 1995 would have updated the Oklahoma General Corporation Act (the “*OGCA*”) and the Oklahoma Limited Liability Company Act (the “*LLC Act*”). House Bill 1996 would have adopted the Revised Uniform Unincorporated Nonprofit Associations Act (the “*RUUNAA*”).

*‑ House Bill 1995 ‑ General*. House Bill1995 was an extensive bill covering over 300 pages and designed to maintain the OGCA and LLC Act.[[44]](#footnote-44) The most significant changes in the bill would have implemented in Oklahoma amendments to the Delaware General Corporation Law (“*DGCL*”) for non-profit corporations and public benefit corporations.[[45]](#footnote-45) Other changes in the bill would have provided for the ratification of defective corporation acts, affirmed that an LLC’s tax status does not affect its status as a legal entity, and affirmed that the fiduciary duties applicable to corporate directors and officers also apply to LLC managers.

*‑ Non-Profit Corporation Provisions*. The OGCA covers both for-profit and non-profit corporations within its scope. Before these changes – which are largely draw from changes to the DGCL ‑ application of the OGCA to non-profit corporations was unclear in many instances. The comprehensive changes in the proposed amendments would fill in the statutory gaps and bring better clarity to non-profit corporations.

The clarifying amendments would begin with a new section that “translates” the terms of the OGCA as they apply to nonstock corporations. For example, while the OGCA provides that a stock corporation has “shareholders” and a “board of directors”, the new section translates those terms as the “members” and “governing body” of the non-profit corporation. References to “stock” become “memberships”. This section also identifies the OGCA sections that will not apply to non-profit corporations, such as those dealing with capital and surplus. Other sections would be changed to clarify the procedures for setting record dates, the calling of special meetings of members and the required vote that must be obtained for corporate action. These clarifications make it easier for nonstock corporations to take action and deal with corporate governance matters.

*‑ Benefit Corporations*. We have previously discussed the trending development of benefit corporations.[[46]](#footnote-46) These are for-profit corporations that combine an explicit public benefit with a for-profit business activity. Delaware adopted “public benefit corporation” statutes in 2013.[[47]](#footnote-47) House Bill 1995 would have brought the Delaware public benefit corporation statutes to Oklahoma.

A public benefit corporation elects “to operate in a responsible and sustainable manner” and identifies a specific public benefit purpose.[[48]](#footnote-48) In decision-making, the directors must balance the economic interests of the shareholders with the best interests of those affected by the corporation’s conduct and the specific public benefit. At least biannually, the directors would report to the shareholders about the corporation’s social and environmental impact and its pursuit of the specific public benefit.

*‑ Fixing Defective Corporate Acts*. The OGCA has no procedure for fixing defective corporate acts. If a corporation fails to follow the statutory procedures – regardless of whether any harm resulted from the failure – it cannot fix the defective act. The amendments would have permitted a board of directors to ratify a defective act. If the act would have required shareholder approval, the shareholders would approve the ratification. The amendments would have also provided for judicial review of the act and ratification and would have empowered the court to order additional steps to fix the defective act. The amendments were patterned upon DGCL changes in 2013.

*‑ Fiduciary Duties for LLC Managers*. Some legal commentary has questioned whether the common law fiduciary duties owed by corporate directors, officers and shareholders also apply to LLC managers and members.[[49]](#footnote-49) House Bill 1995 would have amended the LLC Act to clarify that fiduciary duties applicable to corporations would also apply to LLCs.

*‑ House Bill 1996*. The Revised Uniform Unincorporated Nonprofit Associations Act (the “*RUUNAA*”) would fill a statutory void in the law dealing with unincorporated associations.[[50]](#footnote-50) Oklahoma has no statutory framework for these voluntary associations, which are generally small volunteer organizations such as church groups, youth organizations, neighborhood associations and garden clubs. Their legal status and that of their members is uncertain. Their members can face liability for the obligations of the association. They may have difficulty opening bank accounts. They cannot own real property.

The RUUNAA would address these issues. It would recognize associations as separate legal entities. As such, the associations could own and dispose of property, open accounts and sue and be sued in their own name. The RUUNAA would protect members and managers from personal liability. The association would be responsible for its own obligations. The members and managers would not be responsible solely because they are members or managers of the association. The RUUNAA would provide default rules for the association’s operations – member admission and resignation, roles of members and managers, rights to financial information, and restrictions on personal gain – if the association has no rules of its own. The RUUNAA also has provisions for dissolution and winding up of an association. The RUUNAA does not change existing laws applicable to specific associations, such as churches, or existing laws regarding charitable solicitations.

#### New Oklahoma Cases

Four recent Oklahoma cases deserve mention. Two are shareholder derivative actions that deal with matters leading up to the board and management reshuffling at Chesapeake Energy.[[51]](#footnote-51) A third case deals with charging orders in LLCs. A fourth case deals with the administrative suspension of charters for failure to pay franchise taxes.

The two Chesapeake cases address whether a shareholder must make demand upon the board of directors to remedy the alleged wrong before bringing a derivative action. In *In Re Chesapeake Shareholders Derivative Litigation*,[[52]](#footnote-52) plaintiffs did not make demand arguing that demand was excused. In ***Egleston v. McClendon*,**[[53]](#footnote-53) **plaintiffs made demand.**

In *In Re Chesapeake Shareholders Derivative Litigation*, plaintiffs alleged various wrongs done to Chesapeake by its CEO, Aubrey McClendon, and certain directors.[[54]](#footnote-54) They sought rescission of McClendon’s employment contract, which they asserted was excessive and wasteful.[[55]](#footnote-55) Plaintiffs also sought rescission of Chesapeake’s purchase of McClendon’s art collection and the disgorgement of profits that three directors made on their sales of Chesapeake stock while they allegedly possessed inside information.[[56]](#footnote-56) Defendants moved to dismiss the petition for plaintiffs’ failure to first demand that the board address the alleged wrongdoing.

Plaintiffs’ claims are derivative – the claims relate to wrongs done to Chesapeake and its shareholders, not to the plaintiffs individually. As such, the claims belong to the corporation. Any rights that a shareholder might have to assert the claims are derived from the corporation, and the corporation is by statute managed by its board of directors.[[57]](#footnote-57) This explains why the law generally requires that a shareholder must first make demand on the board to pursue the claims before the shareholder can pursue the claims.

The law has long had an exception to the general demand requirement. If a shareholder can show that making demand would be futile, making demand is excused. This was plaintiffs’ course. In the trial court, the parties agreed that the demand excused exception existed, but disagreed about the applicable standard.[[58]](#footnote-58) Plaintiffs argued that the standard was articulated by the Oklahoma Supreme Court in *Hargrave v. Canadian Valley Electric Coop., Inc*.[[59]](#footnote-59) *Hargrave* involved rate-payers who derivatively sued their electric cooperative and its board of trustees alleging that a power contract authorized by the board was approved improvidently. *Hargrave* seems to hold that the board’s approval of the transactions at issue compromised the board’s independence and is reason enough to excuse demand.

The *Hargrave* holding is a decidedly minority position and defendants urged the trial court to follow the majority position as articulated in Delaware precedent.[[60]](#footnote-60) The majority position holds that mere approval of the transaction at issue is insufficient to excuse demand.[[61]](#footnote-61) A shareholder must show a self-interest or bias that would taint the directors’ judgment.[[62]](#footnote-62) The trial court ostensibly rejected defendants’ position, citing the Oklahoma Supreme Court’s subsequent use of *Hargrave* as precedent.[[63]](#footnote-63) The court went on to review plaintiffs’ additional allegations of bias against the directors.[[64]](#footnote-64) Then the court surprisingly held that demand would not be excused.

The trial court’s holding is somewhat difficult to reconcile with the *Hargrave* holding, which seems to say that board approval is itself sufficient to excuse demand. The trial court clearly wanted more indication of director self-interest or bias to excuse demand. The *Hargrave* analysis is not thorough[[65]](#footnote-65) and it relies heavily on two cases, *Lewis v. Curtis[[66]](#footnote-66)* and *Lewis v. Graves*,[[67]](#footnote-67) that squarely stand for the position that more than mere approval must be shown.[[68]](#footnote-68) If the court believes *Hargrave* intended to follow these cases – but perhaps failed in its application of the law – the trial court’s ruling is more consistent.[[69]](#footnote-69)

On appeal, citing *Hargrave*, the Court of Appeals wrote that the trial court’s determination of whether demand is futile “lies within the discretion of the trial court.”[[70]](#footnote-70) The Court noted that it reviewed the record, “which includes extensive citation to the Delaware law from which Oklahoma derived its General Corporation Act.”[[71]](#footnote-71) It then held that the trial court did not “manifestly err or abuse its discretion” in requiring that plaintiffs make demand.[[72]](#footnote-72) Without further analysis of the applicable standard for determining demand futility, the Court of Appeals decision leaves the matter unresolved. Proponents on either side of the issue can find support in Oklahoma.

As plaintiffs in *In Re Chesapeake Shareholders Derivative Litigation* tried their demand excused strategy, the plaintiff in ***Egleston v. McClendon****[[73]](#footnote-73)* **waited on the outcome. He had made demand** on the Chesapeake board. The board responded that numerous similar lawsuits were pending, as were investigations by the SEC, Department of Justice and the Michigan Attorney General. An internal investigation by the board was also pending. The board chose to defer action on plaintiff’s demand pending the outcomes of these proceedings and investigations. Plaintiff then filed suit derivatively alleging various fiduciary breaches by McClendon and the board and claiming that the board’s decision to defer action was a breach of its business judgment.

The board filed a motion to dismiss. It cited the other pending legal proceedings involving similar claims and asserted that its decision to defer action pending the outcomes of these other legal proceedings was a valid exercise of its business judgment. It argued that Plaintiff’s demand had conceded the board’s independence and Plaintiff had failed to plead facts sufficient to overcome the presumption of propriety afforded by the business judgment rule.

Plaintiff replied that the board’s action “failed to meet the standard of good faith and [the board] did not exercise valid [business] judgment in refusing the demand.”[[74]](#footnote-74) He alleged that the board’s decision was hastily made without an adequate investigation of the claims, and that the board’s independence was compromised since its decision was made in the presence of directors who were involved in the claims.

The trial court held that the board’s decision to defer action was a proper business judgment. Plaintiff appealed.

The Court of Appeals began its analysis by reviewing the nature of shareholder derivative actions, the need for demand, and – when demand is made ‑ the basis for determining whether the board’s response to the demand is appropriate. Regarding the latter, the Court writes that the board’s response is protected by the business judgment rule. The rule presumes that the board “acted on an informed basis, in good faith and in the honest belief that the action taken was in the best interests of the company and its shareholders.”[[75]](#footnote-75) In assessing compliance with the business judgment rule, “the issues before the Court are independence, the reasonableness of its investigation and good faith,” and “when a board refuses a demand, the only issues to be examined are the good faith and reasonableness of its investigation.”[[76]](#footnote-76)

While the general rule is that making demand acknowledges a board’s independence, [[77]](#footnote-77) plaintiff questioned the board’s independence on several grounds. He argued that the board could not properly review McClendon’s allegedly excessive executive compensation because the board had approved his compensation and were tainted by the allegedly excessive compensation they had approved for themselves. But the Court noted these arguments had been made in numerous earlier cases to no avail.[[78]](#footnote-78) A board’s approval of compensation, including its own, “will be upheld unless it cannot be ‘attributed to any rational business purpose.’”[[79]](#footnote-79)

Plaintiff further argued that McClendon’s relationships with the directors compromised their independence. The Court wrote that the law on this issue is also well established. The mere proof of a relationship is insufficient. The facts must show that a director is “beholden” to the other to prove a lack of independence.[[80]](#footnote-80) Plaintiff had not made that showing.

To attack the board’s good faith and reasonableness, Plaintiff argued that the board conducted no investigation, it did not appoint a special litigation committee, and it did not excuse McClendon and certain former Board members from the discussions although allegations of wrongdoing were made again these persons. The Court replied that no specific procedures are required to respond to a demand.[[81]](#footnote-81) In this instance, the board was familiar with the allegations since the allegations were the same as those in earlier legal proceedings and investigations. The board was sufficiently informed to act.[[82]](#footnote-82)

The Court also held that the board’s decision to defer action was supported by valid purposes. Since the same allegations were already contested, deferring action would avoid duplication and conserve resources. In fact, the Court noted, the failure to defer could have compromised the corporation’s position in the other proceedings. For these reasons, the Court found the board’s decision to defer was a “reasonable exercise of business judgment.”[[83]](#footnote-83)

**The last two Oklahoma cases are easier to digest. *Southlake Equipment Co., Inc. v. Henson Gravel & Sand, LLC***[[84]](#footnote-84) **deals with charging orders in limited liability companies. In LLCs, the judgment creditor of an LLC member cannot attach and execute on the interest.**[[85]](#footnote-85) **In a corporation, the judgment creditor of a shareholder can attach and execute on a shareholder’s stock. This distinction between LLCs and corporations rests on the venerable notion that LLC interests, like partnership interests, are presumed to be non-transferable while corporate stock is presumed to be transferable. If execution were permitted, judicial transfers of the LLC interests could occur and the remaining members might face a new member whom they had not anticipated and did not want. To protect these members, the statute provides that the exclusive remedy of a creditor holding a judgment against a debtor member is a charging order.**[[86]](#footnote-86) **A charging order requires the LLC to pay to the judgment creditor any distributions that would otherwise have been paid to the debtor member. The judgment creditor is limited to these distributions. It cannot attach and sell the interest itself.**

**In *Southlake*, Southlake Equipment Company, Inc. obtained an agreed judgment against Melvin Henson and Henson Gravel & Sand, LLC and sought to execute upon the judgment by asking the district court to order the seizure of Melvin Henson’s 24% interest in Econtuchka Erosion Control, LLC, an Oklahoma limited liability company (“*EEC*”). The trial court complied and ordered the transfer of Henson’s entire membership interest in EEC to Southlake. Henson appealed.**

**In its analysis, the Court of Appeals turned to Section 2034 of the Oklahoma LLC Act, which deals with the rights of judgment creditors. The Court highlighted two passages in Section 2034: one stating that a judgment creditor has only the rights of an assignee with respect to the membership interest, and a second stating that a charging order is a judgment creditor’s exclusive remedy with respect to the membership interest.**

**The Court then examined the rights of an assignee. It noted that an assignee can receive a share of the LLC’s profits and losses and its distributions, but cannot vote or otherwise participate in management.**[[87]](#footnote-87) **In other words, an assignee’s rights to participate are limited to a member’s economic interest.**

**The Court noted that the trial court had ordered Henson to transfer his entire interest, not just his economic rights. Trial court erred by not following the statute. The Court further examined EEC’s operating agreement, which require the consent of the non-transferring members to permit a transfer of the interest. Two of members had consented, but one member had not. Without the unanimous consent of the non-transferring members, the operating agreement did not permit the transfer. Here the trial court erred also. The Court remanded for entry of a charging order.**

*Moncrieff-Yeates v. Kane*[[88]](#footnote-88) deals with a corporation’s authority after administrative suspension of its charter for failure to pay franchise taxes. In 2006, K.O.D. Enterprises, Inc. (“*KOD*”) sold property to Moncrieff-Yeates for a note and mortgage. Moncrieff-Yeates defaulted. KOD brought a foreclosure suit and was awarded summary judgment. Moncrieff-Yeates objected and filed post-judgment motions to vacate the judgment, arguing that KOD’s charter had been suspended in 2000 for failure to pay franchise taxes and was never reinstated, and that KOD was precluded from accessing the courts. The matter was eventually taken up by the Court as an application to assume original jurisdiction and request for extraordinary relief.

The Court first examined the tax statute authorizing the charter suspension. The statute provides that during the suspension, (a) the corporation cannot sue or defend, (b) the directors and officers are personally liable for debts incurred with their knowledge, and (c) any contract made during the suspension is voidable.[[89]](#footnote-89) The Court noted that access to the courts could be restored if the corporation were reinstated.[[90]](#footnote-90) But KOD had never paid its delinquent taxes and applied for reinstatement.

KOD argued that its suspension was a dissolution and that it had three years, or more if allowed by the court, to wind up its affairs and resolve its claims in court.[[91]](#footnote-91) The Court disagreed, stating that the suspension was not equivalent to a dissolution. Court wrote that a corporation can be reinstated after suspension, unlike a dissolution which terminates the charter.[[92]](#footnote-92) Further refuting KOD’s argument is the fact that a corporation cannot dissolve without paying its franchise taxes.[[93]](#footnote-93)

The Court is correct in its holding. Once suspended, KOD lacks standing and should be denied access to courts. The Court’s holding is consistent with a long line of Oklahoma cases.[[94]](#footnote-94) The only surprising element in this case was that KOD chose the stand it did and did not pay its delinquent taxes and reinstate.

### Conclusion

While many interesting changes have and will occur at the Federal level, the Oklahoma legislation and cases remind us that state laws matter too. Thousands of new businesses are formed each year in Oklahoma. Add to those the existing businesses. Each of these many businesses depends on Oklahoma statutes and case law to guide their formation and operation. The law guides relationships among owners, between owners and managers, and between the entity and persons with whom it does business. As lawyers, we are uniquely positioned to assist these business and to encourage best business practices. Good corporate governance means better relationships. It also makes for a better marketplace.[[95]](#footnote-95) Markets are more efficient where transparency and trust are found, and transactional risk decreases. The resulting economic benefits help us all.

Gary W. Derrick
November 30, 2014

1. The derivatives markets have expanded in 30 years from a small U.S. market to a globalized market with an outstanding notional value of $691 trillion at June 30, 2014, for OTC derivatives and exchange-traded derivatives. *Semiannual OTC derivatives statistics*, Bank for International Settlement (updated Nov. 6, 2014) (at [http://www.bis.org/statistics/derstats. htm](http://www.bis.org/statistics/derstats.%20htm)). The global private equity market grew from approximately $38 billion in new capital in 1995 to approximately $231 billion in 2013. *Global Private Equity Report for 2014*, Bain & Company (at [http://www.bain.com/publications/ business-insights/global-private-equity-report.aspx](http://www.bain.com/publications/%20business-insights/global-private-equity-report.aspx)). [↑](#footnote-ref-1)
2. *See gen*. Carl Dahlman, *Technology, Globalization, and International Competitiveness*, Industrial Development for the 21st Century (United Nations, 2007) (at [http://www.un.org/esa/ sustdev/publications/industrial\_development/1\_2.pdf](http://www.un.org/esa/%20sustdev/publications/industrial_development/1_2.pdf)); and Thomas Friedman, *The World is Flat* (2005); Robert E. Lucas, Jr., The Industrial Revolution: Past and Future”, *The Region*, The Federal Reserve of Minneapolis (May 2004). [↑](#footnote-ref-2)
3. *See* *Financial Crisis Inquiry Commission Report*, Conclusions of the Financial Crisis Inquiry Commission (January 2011); *see also* Keith Hennessey,Douglas Holtz-Eakin, Bill Thomas and Peter J. Wallison, *Dissenting Statement*,Financial Crisis Inquiry Commission(January 2011). There is a fallacy of belief – at least in an open economy ‑ that good government policies ensure the success of the economy while poor government policies will hurt the economy. Government policy may influence an open economy, but cannot control it. [↑](#footnote-ref-3)
4. The Dodd–Frank Wall Street Reform and Consumer Protection Act (Pub. L. No. 111-203, H.R. 4173) (enacted July 21, 2010) (“*Dodd-Frank*”). Dodd Frank addressed in its 2,300 plus pages the liquidation of “too big to fail” financial institutions, residential mortgage and consumer lending practices, use of derivative securities, proprietary trading by banks, executive compensation, and consumer financial protections. The law firm, Davis Polk, reports that, as of October 1, 2014, 280 Dodd-Frank rulemaking requirement deadlines had passed, of which 115 (41.1%) were still awaiting final rules. In addition, only 220 (55.3%) of the 398 total required rulemakings were finalized, while 95 (23.9%) rulemaking requirements have not yet been proposed. *Dodd-Frank Progress Report*, Davis Polk Resource Center (at http://www.davispolk.com/Dodd-Frank-Rulemaking-Progress-Report/). [↑](#footnote-ref-4)
5. *The JOBS Act: 2014 Mid-Year Update*, a publication of Ernst & Young (Aug. 2014) (at http://www.ey.com/Publication/vwLUAssets/EY-the-JOBS-Act-2014/$FILE/EY-the-JOBS-Act-2014.pdf). [↑](#footnote-ref-5)
6. *See* *Criminalising the American Company*, The Economist (Aug. 30, 2014). The U.S. House of Representative’s Judiciary Committee formed a task force in 2013 to study the over-criminalization of conduct. See <http://judiciary.house.gov/index.cfm/2014/2/house-judiciary-committee-reauthorizes-bipartisan-over-criminalization-task-force>. [↑](#footnote-ref-6)
7. *Id*. The Economist at 22. Drawing from data maintained by University of Virginia law professor, Brandon Garrett, the article shows a dramatic increase in fines against corporations, increases in the number of prosecutions, and a decrease in the number of individuals sentenced. Data at <http://lib.law.virginia.edu/Garrett/prosecution_agreements/home.suphp> and <http://lib.law.virginia.edu/Garrett/plea_agreements/home.php>. In a speech to the New York Bar Association, Judge Jed S. Rakoff criticized the shift away from prosecuting individuals as diminishing the deterrent effect of prosecutions. Reprinted in *The Advocate for Institutional Investors*, a publication of Bernstein Litowitz Berger & Grossmann LLP (Summer 2014) (at [http://www.blbglaw.com/news/publications/data/00171/\_res/id=File1/Adv\_Summer2014\_ Rakoff.pdf](http://www.blbglaw.com/news/publications/data/00171/_res/id%3DFile1/Adv_Summer2014_%20Rakoff.pdf)). [↑](#footnote-ref-7)
8. *Id*. The Economist at 21. *The Economist* article did not include the $4.3 billion in fines paid by six banks, including Citibank and J.P. Morgan, for alleged manipulation of foreign currency markets. *Regulators Fine Global Banks $4.3 Billion in Currency Investigation*, Reuters (Nov. 12, 2014). [↑](#footnote-ref-8)
9. The *New York Times* has reported on alleged violations of the Foreign Corrupt Practices Act by Wal-Mart’s Mexican subsidiary. Elizabeth A. Harris, *After Bribery Scandal, High-Level Departures at Walmart*, N.Y.Times (June 4, 2014); David Barstow, *The Bribery Aisle: How Wal-Mart Got Its Way in Mexico*, N.Y.Times (Dec. 17, 2012). The General Motors problems stem from its handling of faulty ignition switches. Jeff Bennett, *GM Documents Show Senior Executive Had Role in Switch*, Wall St. Jour. (June 26, 2014) (reporting that federal prosecutors have issued grand jury subpoenas concerning the ignition switch defect). [↑](#footnote-ref-9)
10. Law professor John Baker has estimated the number of Federal crimes as nearing 5,000 and the number of regulatory offenses that might be the basis of criminal prosecution is certainly over 300,000. Baker cites an average of 67.17 new crimes annually between 2008 and 2013, including 195 new crimes in 2008. John Baker, “The Crimes on the Books and Committee Jurisdiction”, *Testimony before the Committee on the Judiciary*, U.S. House of Representatives Task Force on Over-Criminalization (July 25, 2014) (at [file:///P:/baker-testimony.pdf](file:///P%3A/baker-testimony.pdf)). These numbers do not account for state criminal statutes. [↑](#footnote-ref-10)
11. Lemos, Margaret H. and Max Minzer, *For-Profit Public Enforcement*, 127 Harv.L.Rev. 853 (2014) (contending that prosecutors “often seek large monetary awards for self-interested reasons divorced from the public interest in deterrence”). [↑](#footnote-ref-11)
12. New York settled charges with five banks in 2012 for $25 billion, the proceeds of which were to have gone to “borrowers harmed by the bank fraud.” Instead, the proceeds were dispersed to several state agencies, some of which played no part in the settlement. The Economist, *supra* at 23-24. In fiscal 2014, the Justice Department announced that it had collected $25 billion in its cases, more than tripling its receipts in 2013. It retained $13.7 billion and remitted the balance to other agencies and entities. Andrew Ramonas, *Feds Collect $24.7B in Penalties – Mostly from Big Banks*, The Blog of Legal Times (Nov. 19, 2014) (at [http://www.nationallawjournal.com/legaltimes/id=1202676887131/Feds-Collect-247B-in-PenaltiesMostly-From-Big-Banks](http://www.nationallawjournal.com/legaltimes/id%3D1202676887131/Feds-Collect-247B-in-PenaltiesMostly-From-Big-Banks)). The annual cost of the 94 U.S. Attorney offices and the Justice Department’s litigation branch was $2.8 billion in 2013. The Economist, *supra* at 21. [↑](#footnote-ref-12)
13. New York has received $5 billion in 2014 from settlements with Credit Suisse, BNP Paribas and Citigroup, which is far more than any other state is receiving. Karen Freifeld and Edward Krudy, *BNP’s Monstrous $9 Billion Fine Is Going Toward . . . New Office Carpets*, Reuters (July 24, 2014) (at <http://www.businessinsider.com/r-bank-settlements-create-windfall-for-us-and-wrangling-over-how-it-is-spent-2014-24>). [↑](#footnote-ref-13)
14. Rakoff, *supra* at fn. 7. [↑](#footnote-ref-14)
15. *Id*. [↑](#footnote-ref-15)
16. Michael Scarcella, *Justice Department Sued over Access to Non-Prosecution Agreement*, Blog of Legal Times (Dec. 2, 2013) (discussing a UVA law clinic’s FOIA (successful) suit to obtain a non-prosecution agreement). The clinic’s suit was filed in conjunction with UVA Prof. Brandon Garrett’s compilation of data regarding deferred prosecution and non-prosecution agreements in light of the “strong public interest in understanding the judicial system and why admitted wrongdoers are not criminally prosecuted”; quoting from the complaint at <http://www.law.virginia.edu/pdf/news/first_amendment_clinic_doj_lawsuit.pdf>). [↑](#footnote-ref-16)
17. 573 U.S. \_\_\_\_, 134 S.Ct. 2751 (2014), *consolidated with* Conestoga Wood Specialties Corp. v. Burwell, No. 13–356. [↑](#footnote-ref-17)
18. The Patient Protection and Affordable Care Act, Pub.L. No. 111–148, 124, Stat. 119 (March 23, 2010). [↑](#footnote-ref-18)
19. Religious Freedom Restoration Act of 1993, Pub.L. No. 103-141, 107 St. 1488 (Nov. 16, 1993). [↑](#footnote-ref-19)
20. Hobby Lobby Stores, Inc. v. Sebelius, 723 F.3d 1114 (10th Cir. 2013). [↑](#footnote-ref-20)
21. Conestoga Wood Specialties Corp. v. Burwell, 724 F.3d 377 (3rd Cir. 2013). The cases were consolidated upon appeal. This paper uses “Hobby Lobby” to refer to the three corporations. [↑](#footnote-ref-21)
22. Trustees of Dartmouth College v. Woodward, 4 Wheat. 518, 636 (1819). [↑](#footnote-ref-22)
23. Citizens United v. Federal Election Comm’n, 558 U. S. 310, 466 (2010) (opinion concurring in part and dissenting in part). [↑](#footnote-ref-23)
24. Justice Alito writes, “A corporation is simply a form of organization used by human beings to achieve desired ends. . . . When rights, whether constitutional or statutory, are extended to corporations, the purpose is to protect the rights of [the corporation’s shareholders, officers, and employees].” *Id.* at 18.

 In the section of his opinion dealing with the corporation’s exercise of religion, Justice Alito carefully refers to Hobby Lobby’s beliefs. Elsewhere, he often refers to the owners’ beliefs as if their beliefs are interchangeable with those of the corporation. *See e.g*., “The owners of the businesses have religious objections” *id.* at 2; “The HHS has provided no reason why the same system cannot be made available when the owners of for-profit corporations have similar religious objections” *id.* at 3; and “[The HHS] requires the Hahns and Greens to engage in conduct that seriously violates their sincere religious belief that life begins at conception” *id.*at 4.

 Justice Kennedy’s brief concurrence is more sweeping. He starts by saying that “all persons have the right to believe or strive to believe in a divine creator and a divine law” *id.* at 1; and “[P]laintiffs deem it necessary to exercise their religious beliefs within the context of their own closely held, for-profit corporations” *id.* at 2 (ignoring that plaintiffs are the corporations, not their owners). Justice Kennedy makes no attempt to distinguish between the beliefs of the owners and those of the entity. [↑](#footnote-ref-24)
25. *Amicus Curiae Brief of Corporate and Criminal Law Professors in Support of Petitioners*, Sebelius v. Hobby Lobby Stores, No. 13-354 *and* Conestoga Wood Specialties Corp. v. Sebelius, No. 13-356 (U.S. Jan. 28, 2014), 2014 WL 333889. [↑](#footnote-ref-25)
26. *Id*. at 2. [↑](#footnote-ref-26)
27. *Id*. [↑](#footnote-ref-27)
28. Stephen M. Bainbridge, *Using Reverse Veil Piercing to Vindicate the Free Exercise Rights of Incorporated Employers*, 16 Green Bag 2d 235 (2013). [↑](#footnote-ref-28)
29. Bainbridge further elaborated his views – and disputed arguments in the *amicus* brief – in *A Critique of the Corporate Law Professors’ Amicus Brief in* Hobby Lobby *and* Conestoga Wood, 100 Virg.L.Rev.Online 1 (March 2014). [↑](#footnote-ref-29)
30. The opinion did not define “closely held” corporation and there is no commonly accepted definition for the term. The agencies that must implement the Court’s opinion have recently proposed rules asking for public comment. Depts. of Treasury, Labor and Health and Human Services have jointly proposed rules open for comment. *See* Depts. of Treasury (RIN 1545-BM39), Labor (RIN 1210-AB67) and Health and Human Services (RIN 0938-AS50), Coverage of Certain Preventive Services under the Affordable Care Act (published Aug. 27, 2014; comments ended Oct. 26, 2014). Under the proposed rules, a for-profit corporation would be eligible for exemption if: (a) none of its stock was publicly traded, and (as alternatives, b-1) specifying a maximum number of owners that it could have, or (b-2) specifying a minimum percentage of a total number of owners who had actual ownership concentrated among them. The public was invited to make suggestions on how a for-profit firm could be required to prove that its owners have established that they do have religious objections to the mandate. If a corporation’s governing structure takes action, in keeping with state law governing corporations, to claim a religious exemption, and advises the government of its objection (by official form or by a simple letter), that would be enough to put the government on notice of the objection, and it would then lead the government to take steps to take over providing access to the services independently of the owners and at no cost to them or to the workers. [↑](#footnote-ref-30)
31. Okla. Stat. tit. 18, §1126. As amended, Section 1126 reads:

“A. In any derivative suit instituted by a shareholder of a corporation, it shall be averred in the petition that the plaintiff was a shareholder of the corporation at the time of the transaction of which the plaintiff complains or that the plaintiff's stock thereafter devolved upon him or her by operation of law.

B. If a derivative action confers a substantial benefit upon the corporation as a result of a compromise or settlement of an action or claim, the court may award the plaintiff reasonable costs, including reasonable attorney fees, and shall direct the plaintiff to remit to the corporation the remainder of all proceeds received.

C. In any derivative action instituted by a shareholder of a domestic or foreign corporation, the court having jurisdiction, upon final judgment, shall require the nonprevailing party or parties to pay the prevailing party or parties the reasonable expenses, including attorney fees, taxable as costs, incurred as a result of such action.”

Subsections B and C were added by the amendment. Subsection A was unchanged. [↑](#footnote-ref-31)
32. Plaintiff attorneys typically receive fees in derivative actions. Derivative actions come within the common fund or common benefit exception to the American rule for attorney fees. *See e.g*., Ams. Mining Corp. v. Theriault, 51 A.3d 1213 (Del. 2012) (Under the common fund doctrine, “a litigant or a lawyer who recovers a common fund for the benefit of persons other than himself or his client is entitled to a reasonable attorney’s fee from the fund as a whole”); and Comment, *Attorney Fees: Attorney Fees, Prevailing Parties, and Judicial Discretion in Oklahoma Practice: How It Is, How It Should Be*, 57 Okla.L.Rev. 947, 949 (2003). Subsection B modifies this practice by requiring a “substantial” benefit. Plaintiff attorneys normally recover if they can show any benefit. *See* Sean J. Griffith, *Correcting Corporate Benefit: How to Fix Shareholder Litigation by Shifting the Doctrine on Fees*, 56 Boston College.L.Rev. 1, 25-27 (forthcoming 2015) (available at www.srn.com/author=32766). [↑](#footnote-ref-32)
33. Shareholder derivative actions may be brought against the directors for breach of fiduciary duty through self-dealing or waste of corporate assets. Shareholders may also sue if the directors have breach duties by failing through neglect to institute proper safeguards that exposed the corporation to “regulatory sanctions, criminal or civil fines, environmental disasters, accounting restatements, misconduct by officers or employees, massive business losses, and innumerable other potential calamities.” This later basis are referred to as “Caremark” claims, after the case *In re Caremark Int’l Inc. Deriv. Litig*., 698 A.2d 959 (Del. Ch. 1996). The M&A derivative claims alleging disclosure weaknesses are typically Caremark claims. [↑](#footnote-ref-33)
34. Robert M. Daines and Olga Koumrian, *Shareholder Litigation Involving Mergers and Acquisitions* (Feb. 2013 update) (available at [https://www.cornerstone.com/CMSPages/GetFile. aspx?guid=9d8fd78f-7807-485a-a8fc-4ec4182dedd6](https://www.cornerstone.com/CMSPages/GetFile.%20aspx?guid=9d8fd78f-7807-485a-a8fc-4ec4182dedd6)). Similar results were reported in Joseph A. Grundfest and Kristen A. Savelle, *The Brouhaha Over Intra-Corporate Forum Selection Provisions: A Legal, Economic, and Political Analysis*, 68 Bus. Law. 325, 335-339(Feb. 2013). [↑](#footnote-ref-34)
35. Andrew J. Pincus, *The Trial Lawyer’s New Merger Tax*, U.S. Chamber Inst. for Legal Reform (Oct. 2012) at 2; and Grundfest and Savelle, *id*. at 328-329 and fn. 20. [↑](#footnote-ref-35)
36. *See* In re Medicis Pharm. Corp. S’holders Litig., Consol. C.A. No. 7857-CS (Del.Ch. Feb. 26, 2014) (refusing a disclosure only settlement because the added disclosure did not “alter the total mix of information” because it “reinforced” management’s recommendation rather than “contradicting” it); *accord* In re Coventry S’holders Litig., C.A. No. 7905-CS (Del.Ch. Aug. 29, 2013); and In re Transatlantic Holdings Inc. S’holders Litig., Consol. C.A. No. 6574-CS (Del.Ch. Feb. 28, 2013). In Texas, the legislature had prohibited the award of attorney fees in class actions that gave the class coupons or similar non-cash consideration, but no money. In *Kazman v. Frontier Oil Corp.*, No. 14-12-000320-CV, 2013 WL 1244376 (Tex. Ct. App. Mar. 28, 2013), a Texas court applied this statute to a disclosure only, merger settlement. The ruling has effectively precluded these types of derivative actions in Texas. [↑](#footnote-ref-36)
37. Shareholder derivative actions were traditionally filed in the jurisdiction of the state of incorporation. In the late 1990’s, plaintiffs began filing in other jurisdictions and now commonly file in multiple jurisdictions when the cases involve large, public corporations. *See* Joseph A. Grundfest, *The History and Evolution of Intra-Corporate Forum Selection Clauses: An Empirical Analysis*, 37 Del.J.Corp.Law 333(2012). [↑](#footnote-ref-37)
38. *See* Boilermakers Local 154 Retirement Fund v. Chevron Corp., 73 A.3d 934 (Del.Ch. 2013) (forum selection bylaws are contractually valid and enforceable in shareholder litigation under Delaware law). Delaware forum selection bylaws have been upheld in Illinois, Louisiana and New York. *See respectively*, Miller v. Beam Inc., 2014-CH-00932 (Ill.Ch.Ct. Mar. 5, 2014), Genoud v. Edgen Group Inc., No. 625,244 (19th Jud.Distr.Ct., East Baton Rouge, La. Jan. 17, 2014), and Hemg Inc. v. Aspen Univ., No. 650457/13, 2013 WL 5958388 (N.Y. Sup.Ct. Nov. 14, 2013). [↑](#footnote-ref-38)
39. 91 A.3d 554 (Del. 2014); see also Hoffman, *Shareholder Suits May Prove Costly*, Wall St. Jour. (May 18, 2104) (reporting on the Delaware court’s upholding of prevailing party bylaw and reporting growth in number of shareholder suits in mergers). [↑](#footnote-ref-39)
40. Delaware 147th General Assembly, Senate Bill 236 (see synopsis attached to bill); Griffith, *supra* at fn. 7, at 5-6. [↑](#footnote-ref-40)
41. Griffith, *id*. at 6-7. [↑](#footnote-ref-41)
42. Two lawsuits were filed against Continental Resources, its CEO and principal shareholder, and certain other directors after it proposed to acquire an affiliate. The suits alleged fiduciary breaches and inadequate disclosure to shareholders who were asked to approve the transaction. See Continental Resources, Inc., Form 10-Q filed Aug. 9, 2012, retrieved from SEC EDGAR website <http://www.sec.gov/edgar.shtml>. The suits were settled after modifications to the disclosures and payment of plaintiff attorney fees. [↑](#footnote-ref-42)
43. Okla. Stat. tit. 18, §1126.C states:

“In any derivative action . . ., the court having jurisdiction, upon final judgment, shall require the non-prevailing party . . . to pay the prevailing party . . . the reasonable expenses, including attorney fees, taxable as costs, incurred as a result of such action.”

Unlike purely private litigation, the shareholder in a derivative action acts in a representative capacity and the action cannot be settled without judicial approval. *See* Howard Erichson, *The Problem of Settlement Class Actions*, 82 Geo.Wash.L.Rev. 951, 968-69 (2014). Thus, there is a “final judgment” even when the action is settled. The subsection also states that the court “shall require” the non-prevailing party to pay. Payment is not a matter of judicial discretion. [↑](#footnote-ref-43)
44. House Bill 1995 was authored by Representative Randy Grau. It was prepared by the Oklahoma General Corporation Act Committee, which is a subcommittee of the Business and Corporate Law Section of the OBA. The Committee drafted the OGCA and the LLC Act and works to maintain the currency of Oklahoma’s business entity legislation. [↑](#footnote-ref-44)
45. Delaware General Corporation Law, tit. 8, chap. 1, Del. Code (“*DGCL*”) The intent in modeling the OGCA after the DGCL was to foster reliance on the large body of Delaware case law, which offers persuasive guidance in Oklahoma. *Price v. Southwestern Bell Tel. Co.*, 812 P.2d 1355 (Okla. 1991); *Woolf v. Universal Fidelity Life Insurance Company*, 849 P.2d 1093 (Okla.Ct.App. 1992) (since the OGCA is based on the DGCL, the OGCA should be interpreted in accordance with Delaware decisions). The continued adoption of the Delaware changes is intended to ensure continued guidance from the Delaware case law. [↑](#footnote-ref-45)
46. Gary W. Derrick, *Recent Developments in Oklahoma Business and Corporate Law – 2012*, OBA 2012 Recent Developments (Day Two). [↑](#footnote-ref-46)
47. 8 Del.C. §§361-368. [↑](#footnote-ref-47)
48. A “public benefit” has “a positive effect (or reduction of negative effects) on one or more categories of persons, entities, communities or interests (other than stockholders in their capacities as stockholders) including, but not limited to, effects of an artistic, charitable, cultural, economic, educational, environmental, literary, medical, religious, scientific or technological nature.” *Id.* §362(b). [↑](#footnote-ref-48)
49. *See* Myron Steele, *Freedom of Contract and Default Contractual Duties in the Delaware Limited Partnerships and Limited Liability Companies*, 46 Am. Bus. L.J. 221 (2009). The vigorous judicial debate in Delaware was resolved by the Delaware legislature’s affirmation that the corporate fiduciary duties apply. Delaware 147th General Assembly, House Bill 126 (eff. Aug. 1, 2013). [↑](#footnote-ref-49)
50. House Bill 1996 was authored by Representative Randy Grau. It was a joint project between the OBA’s Uniform Act Committee and the Oklahoma General Corporation Act Committee, which conformed the language to fit the statutory drafting practices and to accommodate the Secretary of State’s electronic filing system. [↑](#footnote-ref-50)
51. *See gen*., Daniel Gilbert, Joann S. Lublin & Russell Gold, *Chesapeake Overhauls Board*, Wall St. Jour. at B3 (June 22, 2012). [↑](#footnote-ref-51)
52. 2013 OK CIV APP 91. [↑](#footnote-ref-52)
53. **2014 OK CIV APP 11.** [↑](#footnote-ref-53)
54. The appellate decision is a cursory ruling, which attaches the trial court’s more extensive order. This paper’s discussion follows the order. Order Sustaining Defendant’s Motion to Dismiss with Leave to Amend, *In Re Chesapeake Shareholders Derivative Litigation*, Dist. Ct., Okla. Cnty., Okla., CJ-2009-3983 (Feb. 26, 2010) (J. Gray) (the “*Order*”). [↑](#footnote-ref-54)
55. In October 2008, the Chesapeake stock price had declined and McClendon was forced to sell over 90% of his Chesapeake stock to meet margin calls. Soon afterwards, the Compensation Committee met and recommended the renegotiation of McClendon’s employment contract, which was affirmed the following day by the Board of Directors. The contract provided for a $77 million bonus, $20 million in stock awards, and the purchase of McClendon’s art collection for $12 million, which was his cost in the collection. McClendon would not receive the bonus or sale proceeds outright. The bonus or sale proceeds would be applied to fund his share of costs in a program, through which he participated in 2.5% of each well that Chesapeake drilled. The employment contract also contained a “claw-back” provision, in which McClendon must pay back a portion of his compensation, including all of the cash bonus, if he terminated his employment before the end of the five-year term. [↑](#footnote-ref-55)
56. Before disclosure of McClendon’s sale of his stock under the margin calls, three directors –Fred Whittemore, Don Nickles and Charles Maxwell – sold $5.2 million of Chesapeake shares. [↑](#footnote-ref-56)
57. Okla. Stat. tit. 18, §1027.A (“The business and affairs of every corporation . . . shall be managed by or under the direction of a board of directors . . ..”). [↑](#footnote-ref-57)
58. Order, *supra* at pg. 3. [↑](#footnote-ref-58)
59. 1990 OK 43, 792 P.2d 50 (Okla. 1990). [↑](#footnote-ref-59)
60. *See gen*. Rales v. Blasband, 634 A.2d 927, 934 (Del. 1993) (Demand is futile when “the particularized factual allegations of a derivative stockholder complaint create a reasonable doubt that, as of the time the complaint is filed, the board of directors could have properly exercised its independent and disinterested business judgment in responding to a demand.”) [↑](#footnote-ref-60)
61. Citing In re Walt Disney Co. Derivative Litig., 731 A.2d 342 (Del.Ch. 1998), *aff’d with leave to replead*, 746 A.2d 244 (Del. 2000); Good v. Getty Oil Co., 514 1104, 1106 (Del.Ch. 1986); Aronson v. Lewis, 473 A.2d 805 (Del.Ch. 1984); *see also* Lewis v. Curtis, 671 F.2d 779, 785 (3rd Cir. 1982) (“The majority view is that the mere approval of an allegedly injurious corporate transaction, absent self-interest or bias by a majority of the board, is insufficient to excuse demand.”). [↑](#footnote-ref-61)
62. Aronson, *id* at 815 (“[T]he mere threat of personal liability for approving a questioned transaction, standing alone, is insufficient to challenge either the independence or disinterestedness of directors . . ..”). [↑](#footnote-ref-62)
63. Order, *supra* at pg. 4. [↑](#footnote-ref-63)
64. Plaintiffs alleged various ties between the independent directors and McClendon that impaired their ability to exercise independent judgment. [↑](#footnote-ref-64)
65. *Hargrave* can be a paradox. For an exposition of the law, it relies heavily on the two *Lewis* cases, which require more than mere approval of the transaction complained of to excuse demand. Yet if *Hargrave* meant to follow those cases, it misapplies the law. The Court writes, “It was the trustees . . . who negotiated the contract. It was the trustees who allowed the contract to proceed unaltered . . .. We cannot agree that a [demand] would have prodded the trustees to action. They were not disinterested parties, but were directly involved in the transaction.” *Hargrave*, at ¶13. The Court cites no personal financial or business interest affecting the trustees. It cites no conflict of interest between the Canadian Valley trustees and the power supplier. There is no evidence of the type of self-interest or bias that would have excused demand under the two *Lewis* cases or majority position standard. [↑](#footnote-ref-65)
66. 671 F.2d 779, 785 (3rd Cir. 1982), cert. denied, 459 U.S. 880, 103 S.Ct. 176, 74 L.Ed.2d 144 (1982). [↑](#footnote-ref-66)
67. 701 F.2d 245, 248 (2nd Cir. 1983). [↑](#footnote-ref-67)
68. Lewis v. Curtis, *supra* at 785 (“The complaint here alleges that, not only did all the directors participate in and approve of the challenged activity, but the challenged activity is a self-interested transaction”); Lewis v. Graves, *supra* at 248 (“We agree with the district court, however, that absent specific allegations of self-dealing or bias on the part of a majority of the board, mere approval and acquiescence are insufficient to render demand futile”). [↑](#footnote-ref-68)
69. The *Hargrave* opinion cites to the two *Lewis* casesno fewer than seven times and the trial court’s order footnotes *Lewis v Curtis* as “thoroughly [discussing] the approaches different jurisdictions use in determining whether demand is futile.” Order, *supra* at fn. 8. The reliance on these cases suggests judicial support for their adoption. [↑](#footnote-ref-69)
70. *Supra* at ¶4. The Delaware courts no longer defer to the trial court’s discretion in reviewing demand futility cases. In *Brehm v. Eisner*, 746 A.2d 244, 253-54 (Del. 2000), the Delaware Supreme Court overruled seven precedents, including *Aronson*, to the extent those precedents reviewed a shareholder derivative demand or pleading decision by the lower court under an abuse of discretion standard or otherwise suggested deferential appellate review. [↑](#footnote-ref-70)
71. *Id*. at ¶5. [↑](#footnote-ref-71)
72. *Id*. [↑](#footnote-ref-72)
73. **2014 OK CIV APP 11.** [↑](#footnote-ref-73)
74. *Id*. at ¶9. [↑](#footnote-ref-74)
75. *Id*. at ¶8, quoting from Beard v. Love, 2007 OK CIV APP 118. [↑](#footnote-ref-75)
76. *Id*. quoting from Kurtz v. Clark, 2012 OK CIV APP 103. [↑](#footnote-ref-76)
77. A board’s independence is not usually reviewed when demand is refused because the act of making demand acknowledges the board’s ability to act with independence. If some directors are tainted by the alleged misconduct, the board may excuse those directors from deliberations or appoint a special committee comprised solely of independent directors to deal with the demand. If the board were incapable of acting independently, demand would be excuse as futile. *See* Spiegel v. Buntrock, 571 A.2d 767, (Del. 1990) (cited by Egleston at ¶8). [↑](#footnote-ref-77)
78. *Citing* Brehm v. Eisner, 746 A.2d 244, 263 (Del. 2000) (footnotes omitted). [↑](#footnote-ref-78)
79. *Id*. at ¶15, quoting from In re Walt Disney Derivative Litigation, 906 A.2d 27, 74 (Del. 2006) (quoting from Sinclair Oil Corp. v. Levien, 280 A.2d 717, 720 (Del. 1971). [↑](#footnote-ref-79)
80. *Id*. at ¶16, quoting from Rales v. Blasband, 634 A.2d 927, 936 (Del. 1993). [↑](#footnote-ref-80)
81. *Id*. at ¶12. [↑](#footnote-ref-81)
82. *Id*. at ¶13. [↑](#footnote-ref-82)
83. *Id*. at ¶18. [↑](#footnote-ref-83)
84. **2013 OK CIV APP 87, 313 P.3d 289.**  [↑](#footnote-ref-84)
85. The rules for general and limited partnerships are the same as those for LLCs. Okla. Stat. tit. 54, §1-504 (for general partnerships) and §500-703A (for limited partnerships). [↑](#footnote-ref-85)
86. Okla. Stat. tit. 18, §2034, which reads:

“On application to a court of competent jurisdiction by any judgment creditor of a member, the court may charge the membership interest of the member with payment of the unsatisfied amount of the judgment with interest. To the extent so charged, the judgment creditor has only the rights of an assignee of the membership interest. A charging order entered by a court pursuant to this section shall in no event be convertible into a membership interest through foreclosure or other action. This act does not deprive any member of the benefit of any exemption laws applicable to his or her membership interest. This section shall be the sole and exclusive remedy of a judgment creditor with respect to the judgment debtor's membership interest.” [↑](#footnote-ref-86)
87. *Id*. at §2033.A. [↑](#footnote-ref-87)
88. 2013 OK 86, 323 P.3d 215. [↑](#footnote-ref-88)
89. Okla. Stat. tit. 68, §1212. [↑](#footnote-ref-89)
90. *Supra* at ¶16, citing Corman v. H-30 Drilling, Inc., 2001 OK 92, 40 P.3d 1051. [↑](#footnote-ref-90)
91. KOD relied on Section 1099 of the OGCA, which provides that a corporation continues for three years after dissolution for the purpose of winding up its affairs. The three year period can be extended by order of the district court and is extended for the resolution of claims by or against the dissolved corporation begun during the three year period. Okla. Stat. tit. 18, §1099. The trial court appeared to have relied upon this statute to extend KOD’s right to pursue its foreclosure. [↑](#footnote-ref-91)
92. *Supra* at ¶21, citing Williams v. Smith & Nephew, Inc., 2009 OK 36, 212 P.3d 484 (“Under §1212(A), the corporate charter is merely suspended - it is not ‘forfeited,’ ‘cancelled’ or ‘dissolved.’”). *Williams* notes that Section 1212.F provides for the reinstatement of the corporation upon payment of the delinquent fees and holds that “the fact that the corporation may be revived and reinstated reflects that the corporation is not legally dead.” *Id*. at ¶10. The Court [↑](#footnote-ref-92)
93. Section 1096 of the OGCA describes the procedure for dissolution, which requires the filing of a certificate of dissolution with the Secretary of State. Okla. Stat. tit. 18, §1096.D. The Secretary of State will not accept the filing if the corporation is delinquent in the payment of its franchise taxes. *Id*. at §1007.C.2. [↑](#footnote-ref-93)
94. *See e.g.*, Williams v. Smith & Nephew, Inc., *supra*; Corman v. H-30 Drilling, Inc., 2001 OK 92, 40 P.3d 1051; and K.J. McNitt Construction, Inc. v. Economopoulos, 2001 OK CIV APP 45, 23 P.3d 983. s [↑](#footnote-ref-94)
95. *See Down on the Street: A Special Report on American’s Capital Markets*, The Economist (Nov. 25, 2006). [↑](#footnote-ref-95)