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HOUSE DRH10277-MN-11 (03/24)

Short Title: Amend Corp. Gov/Shareholder Derivative Suits. (Public)

Sponsors: Representative Ross.

Referred to:

1 A BILL TO BE ENTITLED
2 AN ACT TO AMEND THE STATUTES RELATING TO THE PROCEDURES IN
3 SHAREHOLDER DERIVATIVE SUITS.

4 The General Assembly of North Carolina enacts:

5 SECTION 1. G.S. 55-7-40.1 reads as rewritten:

6 "§ 55-7-40.1. Definitions.

7 In this Part:

8 (1) ~~"Derivative proceeding" means a Complaint.~~ – A civil complaint filed in a
9 derivative proceeding.

10 (1a) Derivative proceeding. – A civil suit in the right of a domestic corporation
11 or, to the extent provided in G.S. 55-7-47, in the right of a foreign
12 corporation.

13 (2) ~~"Shareholder" has Shareholder.~~ – Has the same meaning as in G.S. 55-1-40
14 and includes a beneficial owner whose shares are held in a voting trust or
15 held by a nominee on the beneficial owner's behalf."

16 SECTION 2. G.S. 55-7-42 reads as rewritten:

17 "§ 55-7-42. ~~Demand.~~Demand; rejection of demand.

18 (a) No shareholder may commence a derivative proceeding until:

19 (1) A written demand has been made upon the corporation to take suitable
20 action; and

21 (2) 90 days have expired from the date the demand was made ~~unless, unless one~~
22 of the following applies:

23 a. Prior ~~prior~~ to the expiration of the 90 days, the shareholder was
24 notified that the corporation rejected the ~~demand, or unless demand.~~

25 b. The shareholder alleges with particularity, and the court determines,
26 that imminent irreparable injury to the corporation would result by
27 waiting for the expiration of the 90-day period.

28 (b) The failure of the corporation to respond to a demand shall not be deemed to be a
29 decision or acknowledgement that the derivative proceeding is in the best interest of the
30 corporation or should proceed, and such a failure does not compromise or affect any of the
31 rights of the corporation under this Part or other applicable law.

32 (c) In the event that the corporation rejects a demand, the corporation shall promptly
33 provide the shareholder written notice of the rejection. The notice must include a summary of
34 the reasons for the rejection of the demand and the identity of the directors of the corporation
35 who approved the rejection of the demand."

36 SECTION 3. G.S. 55-7-43 reads as rewritten:



1 **"§ 55-7-43. Stay of proceedings.**

2 (a) If the corporation commences or has commenced an inquiry into the allegations set
3 forth in ~~the a demand or complaint, complaint as permitted by G.S. 55-7-44(a)(2) or (3), except~~
4 ~~for motions and submittals in connection with the inquiry and such discovery as the court may~~
5 expressly permit pursuant to G.S. 55-7-44(a)(2) or (3), the court may shall stay a derivative
6 proceeding for a reasonable time period of time ~~the court deems appropriate~~ while the
7 corporation completes its inquiry and while the results of the inquiry are presented to and
8 considered by the court.

9 (b) The corporation or other defendants in a derivative proceeding may move to dismiss
10 a complaint under G.S. 55-7-44(a)(4) or (5) at any time (i) prior to, during, or subsequent to
11 any inquiry by the corporation into the allegations set forth in a demand or complaint, and (ii)
12 either before or after the court's ruling on any motion that may be brought under
13 G.S. 55-7-44(a)(2) or (3). If a corporation or any other defendant in a derivative proceeding
14 files a motion to dismiss under G.S. 55-7-44(a)(4) or (5), all discovery in the proceeding is
15 stayed until the motion to dismiss is denied, with the exception of any discovery expressly
16 permitted by the court pursuant to G.S. 55-7-44(a)(2) or (3).

17 (c) Nothing in this section restricts the right of a shareholder to inspect records of the
18 corporation as provided in Article 16 of this Chapter."

19 **SECTION 4.** G.S. 55-7-44 reads as rewritten:

20 **"§ 55-7-44. Dismissal.**

21 (a) ~~The court shall dismiss a derivative proceeding on motion of the corporation if one~~
22 ~~of the groups specified in subsection (b) or (f) of this section determines in good faith after~~
23 ~~conducting a reasonable inquiry upon which its conclusions are based that the maintenance of~~
24 ~~the derivative proceeding is not in the best interest of the corporation.~~

25 (b) ~~Unless a panel is appointed pursuant to subsection (f) of this section, the inquiry and~~
26 ~~determination shall be made by:~~

27 (1) ~~A majority vote of independent directors present at a meeting of the board of~~
28 ~~directors if the independent directors constitute a quorum; or~~

29 (2) ~~A majority vote of a committee consisting of two or more independent~~
30 ~~directors appointed by majority vote of independent directors present at a~~
31 ~~meeting of the board of directors, whether or not the independent directors~~
32 ~~constituted a quorum.~~

33 (c) ~~For purposes of this section, none of the following factors by itself shall cause a~~
34 ~~director to be considered not independent:~~

35 (1) ~~The nomination or election of the director by persons who are defendants in~~
36 ~~the derivative proceeding or against whom action is demanded;~~

37 (2) ~~The naming of the director as a defendant in the derivative proceeding or as~~
38 ~~a person against whom action is demanded; or~~

39 (3) ~~The approval by the director of the act being challenged in the derivative~~
40 ~~proceeding or demand if the act resulted in no personal benefit to the~~
41 ~~director.~~

42 (d) ~~If a derivative proceeding is commenced after a determination has been made~~
43 ~~rejecting a demand by a shareholder, the complaint shall allege with particularity facts~~
44 ~~establishing that the requirements of subsection (a) of this section have not been met.~~
45 ~~Defendants may make a motion to dismiss a complaint under subsection (a) of this section for~~
46 ~~failure to comply with this subsection. Prior to the court's ruling on such a motion to dismiss,~~
47 ~~the plaintiff shall be entitled to discovery only with respect to the issues presented by the~~
48 ~~motion and only if and to the extent that the plaintiff has alleged such facts with particularity.~~
49 ~~The preliminary discovery shall be limited solely to matters germane and necessary to support~~
50 ~~the facts alleged with particularity relating solely to the requirements of subsection (a) of this~~
51 ~~section.~~

1 (e) ~~If a majority of the board of directors does not consist of independent directors at~~
2 ~~the time the determination is made, the corporation shall have the burden of proving that the~~
3 ~~requirements of subsection (a) of this section have been met. If a majority of the board of~~
4 ~~directors consists of independent directors at the time the determination is made, the plaintiff~~
5 ~~shall have the burden of proving that the requirements of subsection (a) of this section have not~~
6 ~~been met.~~

7 (f) ~~The court may appoint a panel of one or more independent persons upon motion of~~
8 ~~the corporation to make a determination whether the maintenance of the derivative proceeding~~
9 ~~is in the best interest of the corporation. The plaintiff shall have the burden of proving that the~~
10 ~~requirements of subsection (a) of this section have not been met.~~

11 (a) The court shall dismiss a derivative proceeding on motion of the corporation or any
12 other defendant in the derivative proceeding in any of the following circumstances:

13 (1) A corporation institutes or has instituted its own proceeding to address or
14 seek relief on account of, or with respect to, the events, transactions, or
15 occurrences set forth in the demand or the complaint.

16 (2) Prior to the commencement of the derivative proceeding, a majority of the
17 qualified directors of the corporation or a majority of a committee comprised
18 of one or more qualified directors has determined, following a reasonable
19 inquiry, that the institution of a derivative proceeding is not in the best
20 interests of the corporation and rejects the shareholder's demand. If the
21 complaint alleges with particularity facts demonstrating that the
22 determination was not approved either by a majority of the qualified
23 directors or a majority of a committee comprised of one or more qualified
24 directors acting in good faith and after a reasonable inquiry, the court may
25 permit discovery limited to the facts that are alleged with particularity. The
26 court shall dismiss the proceeding if the plaintiff fails to sustain the burden
27 of showing by clear and convincing evidence that the determination was not
28 so approved.

29 (3) After commencement of a derivative proceeding, a majority of the qualified
30 directors of the corporation, a majority of a committee comprised of one or
31 more qualified directors, or a majority of a panel appointed by the court
32 under subsection (e) of this section has determined, following a reasonable
33 inquiry, that the maintenance of the derivative proceeding is not in the best
34 interests of the corporation and authorizes the corporation to request
35 dismissal of the derivative proceeding. If in response to the motion
36 requesting dismissal, the plaintiff alleges with particularity facts
37 demonstrating that the determination was not approved by a majority of the
38 qualified directors, a majority of a committee comprised of one or more
39 qualified directors, or a majority of the court-appointed panel acting in good
40 faith and after a reasonable inquiry, the court may permit discovery limited
41 to the facts that are alleged with particularity. The court shall dismiss the
42 proceeding if the plaintiff fails to sustain the burden of showing by clear and
43 convincing evidence that the determination was not so approved.

44 (4) The shareholder has failed to comply with the requirements of
45 G.S. 55-7-42(a).

46 (5) The court determines that the proceeding should be dismissed for failure to
47 state a claim upon which relief can be granted, or for any other reason
48 enumerated in G.S. 1A-1, Rule 12.

49 (b) A court's decision not to dismiss a derivative proceeding under subdivision (a)(2) of
50 this section does not preclude the corporation from commencing an inquiry into the allegations
51 set forth in a complaint and seeking dismissal thereof as provided in subdivision (a)(3) of this

1 section, nor does it preclude the corporation or any defendant in a derivative proceeding from
2 seeking dismissal under subdivision (a)(4) or (5) of this section.

3 (c) An inquiry in response to a demand or complaint may be conducted by directors,
4 officers, employees, attorneys, or agents of the corporation acting at the direction of the
5 corporation, its board of directors or a committee thereof. In determining whether such an
6 inquiry is reasonable, the court shall consider, among other relevant matters, the scope of the
7 inquiry relative to the particularity of the allegations made in the demand or complaint, as the
8 case may be.

9 (d) A board of directors may appoint a committee of one or more qualified directors,
10 even though a majority of the board of directors is not comprised of qualified directors, so long
11 as the board of directors acts with approval of a majority of the qualified directors.

12 (e) Upon motion by the corporation, the court may appoint a panel of one or more
13 individuals to direct an inquiry and make a determination whether the maintenance of the
14 derivative proceeding is in the best interests of the corporation.

15 (f) The following definitions apply in this section:

16 (1) Material interest. – An actual or potential benefit or detriment (other than
17 one which would devolve on the corporation or the shareholders generally)
18 that would reasonably be expected to impair the objectivity of a director's
19 judgment when participating in the action to be taken.

20 (2) Material relationship. – A familial, financial, professional, employment, or
21 other relationship that would reasonably be expected to impair the
22 objectivity of a director's judgment when participating in the action to be
23 taken.

24 (3) Qualified director. – A director of the corporation who, at the time action is
25 taken that relates to this Part, does not have a material interest in the
26 outcome of the proceeding or a material relationship with a person who has
27 such an interest. The presence of one or more of the following circumstances
28 does not automatically prevent a director from being a qualified director:

29 a. Nomination or election of the director to the current board by any
30 director who is not a qualified director with respect to the matter (or
31 by any person that has a material relationship with that director),
32 acting alone or participating with others.

33 b. Service as a director of another corporation of which a director who
34 is not a qualified director with respect to the matter (or any individual
35 who has a material relationship with that director) is or was also a
36 director.

37 c. Status as a named defendant, as a director against whom action is
38 demanded, or as a director who approved the conduct being
39 challenged."

40 **SECTION 5.** G.S. 55-7-45(a) reads as rewritten:

41 "(a) A derivative proceeding may not be discontinued or settled without the court's
42 approval. If the court determines that a proposed discontinuance or settlement will substantially
43 affect the interests of the corporation's shareholders or a class of shareholders, the court shall
44 direct that notice be given to the shareholders affected. Notice may be provided in any method
45 approved by the court, including, for a public corporation, by publication of a press release
46 through a news release service with national distribution."

47 **SECTION 6.** G.S. 55-7-47 reads as rewritten:

48 **"§ 55-7-47. Applicability to foreign corporations.**

49 In any derivative proceeding in the right of a foreign corporation, the matters covered by
50 this Part shall be governed by the laws of the jurisdiction of incorporation of the foreign
51 corporation except for the matters governed by G.S. 55-7-43, 55-7-45, and 55-7-46. The

1 repose period in G.S. 55-7-48(2) applies to a foreign corporation if its principal office is located
2 in North Carolina."

3 **SECTION 7.** G.S. 55-7-48 reads as rewritten:

4 "**§ 55-7-48. Suits against directors of public corporations.**

5 In addition to the requirements of this Part, the plaintiff in ~~an action~~ a derivative proceeding
6 brought on behalf of a corporation that is a public corporation ~~at the time of the action~~ against
7 one or more of its directors for monetary damages shall:

- 8 (1) Allege, and it must appear, that each plaintiff has been a shareholder or
9 holder of a beneficial interest in shares of the corporation for at least one
10 year;
- 11 (2) Bring the action within two years of the date of the transaction of which the
12 plaintiff complains; and
- 13 (3) If the court orders, upon motion made by the corporation at any time prior to
14 the final resolution of the proceeding, execute and deposit with the clerk of
15 court a written undertaking with sufficient surety, approved by the court, to
16 indemnify the corporation against any and all expenses reasonably expected
17 to be incurred by the corporation in connection with the proceeding,
18 including attorneys' fees and any expenses arising by way of indemnity. In
19 determining whether to require such an undertaking, the court shall consider
20 whether the derivative proceeding appears to have been commenced or
21 maintained without reasonable cause or for an improper purpose."

22 **SECTION 8.** G.S. 55-8-25(b1) is repealed.

23 **SECTION 9.** This act becomes effective October 1, 2015, and applies to demands
24 made and complaints filed on or after that date.