

SHAREHOLDER DERIVATIVE ACTIONS

2000 GENERAL SESSION

STATE OF UTAH

Sponsor: Greg J. Curtis

AN ACT RELATING TO CORPORATIONS; AMENDING PROVISIONS RELATED TO
DERIVATIVE PROCEEDINGS; AND MAKING TECHNICAL CHANGES.

This act affects sections of Utah Code Annotated 1953 as follows:

AMENDS:

16-10a-740, as enacted by Chapter 277, Laws of Utah 1992

Be it enacted by the Legislature of the state of Utah:

Section 1. Section **16-10a-740** is amended to read:

16-10a-740. Procedure in derivative proceedings.

(1) As used in this section:

(a) "derivative proceeding" means a civil suit in the right of:

(i) a domestic corporation; or

(ii) to the extent provided in Subsection (7), a foreign corporation; and

(b) "shareholder" includes a beneficial owner whose shares are held:

(i) in a voting trust; or

(ii) by a nominee on the beneficial owner's behalf.

~~(2) A [person] shareholder may not commence or maintain a derivative proceeding
[in the right of a domestic or foreign corporation] unless the [person] shareholder:~~

~~(a) (i) was a shareholder of the [domestic or foreign] corporation [when the transaction]
at the time of the act or omission complained of [occurred]; or [unless the person]~~

~~(ii) became a shareholder through transfer by operation of law from one who was a
shareholder at [that] the time of the act or omission complained of; and~~

~~(b) fairly and adequately represents the interests of the corporation in enforcing the right
of the corporation.~~

28 (3) (a) A shareholder may not commence a derivative proceeding until:

29 (i) a written demand has been made upon the corporation to take suitable action; and

30 (ii) 90 days have expired from the date the demand described in Subsection (3)(a)(i) is
31 made unless:

32 (A) the shareholder is notified before the 90 days have expired that the demand has been
33 rejected by the corporation; or

34 (B) irreparable injury to the corporation would result by waiting for the expiration of the
35 90-day period.

36 ~~[(2)]~~ (b) A complaint in a derivative proceeding [brought in the right of a corporation
37 must] shall be:

38 (i) verified; and

39 (ii) allege with particularity the demand made[~~-, if any,~~] to obtain action by the board of
40 directors [and either that the demand was refused or ignored or why the complainant did not make
41 the demand. Whether or not a demand for action was made, if the corporation commences an
42 investigation of the charges made in the demand or complaint, the].

43 (c) A derivative proceeding shall comply with the procedures of Utah Rules of Civil
44 Procedure, Rule 23.1.

45 (d) The court [may] shall stay any derivative proceeding until the [investigation] inquiry
46 is completed[;] h **AND FOR SUCH ADDITIONAL PERIOD AS THE COURT CONSIDERS**

46a **APPROPRIATE h if:**

47 (i) the corporation commences an inquiry into the allegations made in the demand or
48 complaint; and

49 (ii) a person or group described in Subsection (4) is conducting an active review of the
50 allegations in good faith.

51 (e) If a corporation proposes to dismiss a derivative proceeding pursuant to Subsection
52 (4)(a), discovery by a shareholder following the filing of the derivative proceeding in accordance
53 with this section:

54 (i) shall be limited to facts relating to:

55 (A) whether the person or group described in Subsection (4)(b) or (4)(f) is independent and
56 disinterested;

57 (B) the good faith of the inquiry and review by the person or group described in Subsection
58 (4)(b) or (4)(f); and

59 (C) the reasonableness of the procedures followed by the person or group described in
60 Subsection (4)(b) or (4)(f) in conducting its review; and

61 (ii) may not extend to any facts or substantive matters with respect to the act, omission,
62 or other matter that is the subject matter of ~~h [the action in] h~~ the derivative proceeding.

63 (4) (a) A derivative proceeding shall be dismissed by the court on motion by the
64 corporation if a person or group specified in Subsections (4)(b) or (4)(f) determines in good faith
65 after conducting a reasonable inquiry upon which its conclusions are based that the maintenance
66 of the derivative proceeding is not in the best interests of the corporation.

67 (b) Unless a panel is appointed pursuant to Subsection (4)(f), the determination in
68 Subsection (4)(a) shall be made by:

69 (i) a majority vote of independent directors present at a meeting of the board of directors
70 if the independent directors constitute a quorum; or

71 (ii) a majority vote of a committee consisting of two or more independent directors
72 appointed by a majority vote of independent directors present at a meeting of the board of
73 directors, whether or not ~~h [the] SUCH h~~ independent directors appointing ~~h [for] h~~ the committee
73a constituted a
74 quorum.

75 (c) None of the following shall by itself cause a director to be considered not independent
76 for purposes of this section:

77 (i) the nomination or election of the director by persons:

78 (A) who are defendants in the derivative proceeding; or

79 (B) against whom action is demanded;

80 (ii) the naming of the director as:

81 (A) a defendant in the derivative proceeding; or

82 (B) a person against whom action is demanded; or

83 (iii) the approval by the director of the act being challenged in the derivative proceeding
84 or demand if the act resulted in no personal benefit to the director.

85 (d) If a derivative proceeding is commenced after a determination has been made rejecting
86 a demand by a shareholder, the complaint shall allege with particularity facts establishing either:

87 (i) that a majority of the board of directors did not consist of independent directors at the
88 time the determination was made; or

89 (ii) that the requirements of Subsection (4)(a) have not been met.

90 (e) (i) If a majority of the board of directors does not consist of independent directors at
91 the time the determination is made rejecting a demand by a shareholder, the corporation has the
92 burden of proving that the requirements of Subsection (4)(a) have been met.

93 (ii) If a majority of the board of directors consists of independent directors at the time the
94 determination is made rejecting a demand by a shareholder, the plaintiff has the burden of proving
95 that the requirements of Subsection (4)(a) have not been met.

96 (f) (i) The court may appoint a panel of one or more independent persons upon motion by
97 the corporation to make a determination whether the maintenance of the derivative proceeding is
98 in the best interests of the corporation.

99 (ii) If the court appoints a panel under Subsection (4)(f)(i), the plaintiff has the burden of
100 proving that the requirements of Subsection (4)(a) have not been met.

101 (g) A person may appeal from an interlocutory order of a court that grants or denies a
102 motion to dismiss brought pursuant to Subsection (4)(a).

103 ~~[(3)]~~ (5) (a) A derivative proceeding [commenced under this section] may not be
104 discontinued or settled without the court's approval.

105 (b) If the court determines that a proposed discontinuance or settlement will substantially
106 affect the [interest] interests of the corporation's shareholders or a class of shareholders, the court
107 shall direct that notice be given to the shareholders affected.

108 ~~[(4)]~~ (6) On termination of the derivative proceeding the court may [require] order:

109 (a) the corporation to pay the plaintiff's reasonable expenses, including counsel fees,
110 incurred in the proceeding, if it finds that the proceeding has resulted in a substantial benefit to the
111 corporation;

112 (b) the plaintiff to pay any defendant's reasonable expenses, including counsel fees,
113 incurred in defending the proceeding, if it finds that the proceeding was commenced or maintained:

114 (i) without reasonable cause[-]; or

115 (ii) for an improper purpose; or

116 (c) a party to pay an opposing party's reasonable expenses, including counsel fees, incurred
117 because of the filing of a pleading, motion, or other paper, if it finds that the pleading, motion, or
118 other paper was:

119 h [(ii)] (i) h (A) not well grounded in fact, after reasonable inquiry; or

120 (B) not warranted by existing law or a good faith argument for the extension, modification,

121 or reversal of existing law; and

122 h [(iii)] (ii) h interposed for an improper purpose, such as to:

123 (A) harass;

124 (B) cause unnecessary delay; or

125 (C) cause needless increase in the cost of litigation.

126 ~~[(5) A proceeding pursuant to this section shall comply with the procedures set forth in~~
127 ~~Rule 23.1 of the Utah Rules of Civil Procedure.]~~

128 ~~[(6) For purposes of this section, "shareholder" includes a beneficial owner whose shares~~
129 ~~are held in a voting trust or held by a nominee on behalf of the beneficial owner.]~~

130 (7) (a) In any derivative proceeding in the right of a foreign corporation, the matters
131 covered by this section shall be governed by the laws of the jurisdiction of incorporation of the
132 foreign corporation except for Subsections (3)(c), (3)(d), (5), and (6), which are procedural and not
133 matters relating to the internal affairs of the foreign corporation.

134 (b) In the case of matters relating to a foreign corporation under Subsection (3)(c):

135 (i) references to a person or group described in Subsection (4) are considered to refer to
136 a person or group entitled under the laws of the jurisdiction of incorporation of the foreign
137 corporation to review and dispose of a derivative proceeding; and

138 (ii) the standard of review of a decision by the person or group to dismiss the derivative
139 proceeding is to be governed by the laws of the jurisdiction of incorporation of the foreign
140 corporation.

Legislative Review Note

as of 1-21-00 10:50 AM

A limited legal review of this legislation raises no obvious constitutional or statutory concerns.

Office of Legislative Research and General Counsel