

P.L.2013, CHAPTER 42, *approved April 1, 2013*
Assembly, No. 3123 (*First Reprint*)

1 **AN ACT** concerning derivative proceedings and shareholder class
2 actions, supplementing chapter 3 of Title 14A of the New Jersey
3 Statutes, and repealing N.J.S.14A:3-6.

4

5 **BE IT ENACTED** by the Senate and General Assembly of the State
6 of New Jersey:

7

8 1. As used in this section:

9 “Derivative proceeding” means a civil suit in the right of a
10 domestic corporation.

11 “Shareholder” includes a beneficial owner whose shares are held
12 in a voting trust or held by a nominee on the beneficial owner’s
13 behalf.

14 “Shareholder class action” means a civil suit by a shareholder
15 against a domestic corporation or its directors or officers which
16 alleges a breach of any duty by the directors or officers or the
17 corporation which is imposed in whole or in part by statutory or
18 common law of the State of New Jersey and seeks a right, remedy,
19 or damages on behalf of a class of the domestic corporation’s
20 shareholders.

21

22 2. A shareholder may not commence or maintain a derivative
23 proceeding unless the shareholder:

24 (1) was a shareholder of the corporation at the time of the act or
25 omission complained of or became a shareholder through transfer
26 by operation of law from one who was a shareholder at that time
27 and remains a shareholder throughout the derivative proceeding;
28 and

29 (2) fairly and adequately represents the interests of the
30 corporation in enforcing the right of the corporation.

31

32 3. No shareholder may commence a derivative proceeding
33 until:

34 (1) a written demand has been made upon the corporation to
35 take suitable action; and

36 (2) 90 days have expired from the date the demand was made
37 unless the shareholder has earlier been notified that the demand has

EXPLANATION – Matter enclosed in bold-faced brackets [thus] in the above bill is not enacted and is intended to be omitted in the law.

Matter underlined thus is new matter.

Matter enclosed in superscript numerals has been adopted as follows:

¹Assembly ACE committee amendments adopted September 24, 2012.

1 been rejected by the corporation or unless irreparable injury to the
2 corporation would result by waiting for the expiration of the 90-day
3 period.

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5 4. If the corporation commences an inquiry into the allegations
6 made in the demand or complaint, the court may stay any derivative
7 proceeding as the court deems appropriate.

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9 5. (1) Subject to subsection (5) of this section, a derivative
10 proceeding shall be dismissed by the court on motion by the
11 corporation if the court finds that:

12 (a) the person or group specified in paragraphs (a) or (b) of
13 subsection (2) of this section or subsection (6) of this section has
14 determined in good faith, after conducting a reasonable inquiry
15 upon which its conclusions are based, that the maintenance of the
16 derivative proceeding is not in the best interests of the corporation;
17 or

18 (b) the shareholders specified in paragraph (c) of subsection (2)
19 of this section have voted to terminate the derivative proceeding.

20 (2) Unless a panel is appointed pursuant to subsection (6) of this
21 section, the determination in subsection (1) of this section shall be
22 made by:

23 (a) a majority vote of independent directors present at a meeting
24 of the board of directors if the independent directors constitute a
25 quorum;

26 (b) a majority vote of a committee consisting of one or more
27 independent directors appointed by majority vote of independent
28 directors, or one independent director if the board consists of only
29 one independent director, present at a meeting of the board of
30 directors, regardless of whether those independent directors
31 constitute a quorum of the board; or

32 (c) the vote of the holders of a majority of the outstanding
33 shares entitled to vote, not including shares owned by or voted
34 under the control of a shareholder or related person who has or had
35 a material beneficial financial interest in the act or omission
36 complained of or other interest therein that would reasonably be
37 expected to exert an influence on that shareholder's or related
38 person's judgment if called upon to vote in the determination.

39 (3) If a derivative proceeding is commenced after a
40 determination has been made rejecting a demand by a shareholder,
41 the complaint shall allege with particularity facts establishing '[:

42 (a) that¹ a majority of the board of directors, or all members of
43 a **['Committee] committee**¹, which in either case determined the
44 matter, did not consist of independent directors at the time the
45 determination was made **['];** or

46 (b) the requirements of subsection (1) of this section have not
47 been met; or

48 (c) **both**¹ .

1 (4) If a majority of the board of directors consisted of
2 independent directors at the time the determination in subsection (1)
3 of this section was made or if the determination is made by
4 shareholders, the plaintiff shall have the burden of proving that the
5 requirements of subsection (1) of this section have not been met. If
6 a majority of the board of directors does not consist of independent
7 directors at the time the determination by independent directors is
8 made, the corporation shall have the burden of proving that the
9 requirements of subsection (1) of this section have been met.

10 (5) (a) If the corporation moves to dismiss the derivative
11 proceeding, it shall make a written filing with the court setting
12 forth, among other things, facts to show:

13 (i) whether or not a majority of the board of directors was
14 independent at the time of the determination by the independent
15 director or directors; and

16 (ii) that the independent director or directors made the
17 determination in good faith after conducting a reasonable inquiry
18 upon which the conclusions are based.

19 (b) Following a motion filed pursuant to paragraph (a) of this
20 subsection, the court shall dismiss the derivative suit unless:

21 (i) the court finds that the requirements of subsection (1) of this
22 section have not been met, taking into account the burden of proof
23 under subsections (4) or (6) of this section; or

24 (ii) the plaintiff, in its complaint, an amended complaint, or in a
25 written filing with the court, has alleged with particularity facts
26 rebutting the facts contained in the corporation's filing.

27 (c) All discovery proceedings shall be stayed upon the filing by
28 the corporation of its motion to dismiss and the filing required by
29 this subsection until the notice of entry of the order ruling on the
30 motion. Notwithstanding the foregoing stay of discovery, the court,
31 on motion and after a hearing, may order that specified and limited
32 discovery be conducted if plaintiffs make a good cause showing of
33 alleged facts which evidence a lack of independence by the person
34 or group making the determination for the corporation or a lack of a
35 good faith determination. Limited discovery shall not include the
36 work product, privileged communications, or testimony of attorneys
37 who advised or assisted the person or group making the
38 determination.

39 (6) Upon motion by the corporation, the court may appoint a
40 panel of one or more individuals to make a determination whether
41 the maintenance of the derivative proceeding is in the best interests
42 of the corporation. The plaintiff shall have the burden of proving to
43 the panel that the requirements of subsection (1) of this section have
44 not been met.

45 (7) (a) A director shall be considered independent for the
46 purposes of this section if the director has:

47 (i) no economic interest in the challenged act or transaction
48 material to him or her, other than an economic interest that is shared
49 by all shareholders generally; and

1 (ii) no material, personal, or business relationships with the
2 defendant directors or officers who have a material interest in the
3 act or transaction challenged.

4 (b) None of the following shall by itself cause a director to be
5 considered not independent for the purposes of this section:

6 (i) the nomination or election of the director by a person who is
7 a defendant in the derivative proceeding or against whom action is
8 demanded;

9 (ii) the naming of the director as a defendant in the derivative
10 proceeding or as a person against whom action is demanded; or

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

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15 6. A derivative proceeding or a shareholder class action may
16 not be discontinued or settled without the court's approval. If the
17 court determines that a proposed discontinuance or settlement will
18 substantially affect the interests of the corporation's shareholders or
19 a class of shareholders, the court shall direct that notice be given to
20 the shareholders affected.

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22 7. On termination of a derivative proceeding or a shareholder
23 class action the court may:

24 (1) order the corporation to pay the plaintiff's expenses incurred
25 in the proceeding if it finds that the proceeding has resulted in a
26 substantial benefit to the corporation;

27 (2) order the plaintiff to pay any defendant's expenses incurred
28 in defending the proceeding if it finds that the proceeding was
29 commenced or maintained without the exercise of reasonable
30 diligence by the plaintiff or without reasonable cause or for an
31 improper purpose; or

32 (3) order a party to pay an opposing party's expenses incurred
33 because of the filing of a pleading, motion or other paper, if it finds
34 that the pleading, motion or other paper was not well grounded in
35 fact, after reasonable inquiry, or warranted by existing law or a
36 good faith argument for the extension, modification or reversal of
37 existing law and was interposed for an improper purpose, such as to
38 harass or cause unnecessary delay or needlessly increase in the cost
39 of litigation.

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41 8. In any derivative proceeding or shareholder class action
42 instituted by a shareholder or shareholders holding less than 5% of
43 the outstanding shares of any class or series of the corporation,
44 unless the shares have a market value in excess of \$250,000, the
45 corporation in whose right the action is brought shall be entitled at
46 any time before final judgment to require the plaintiff or plaintiffs
47 to give security for the reasonable expenses, including fees of
48 attorneys, that may be incurred by it in connection with the action
49 or may be incurred by other parties named as defendant for which it

1 may become legally liable. Market value shall be determined as of
2 the date that the plaintiff institutes the action or, in the case of an
3 intervener, as of the date that the intervener becomes a party to the
4 action. The corporation shall have recourse to that security in that
5 amount which the court having jurisdiction shall determine upon the
6 termination of the action in accordance with section 7 of P.L. ,
7 c. (C.)(pending before the Legislature as this bill).

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9 9. In any derivative proceeding or shareholder class action, the
10 provisions of P.L. , c. (C.)(pending before the Legislature
11 as this bill) shall apply to actions brought in state or federal court
12 both within and outside of the State of New Jersey if the provisions
13 of P.L. , c. (C.)(pending before the Legislature as this bill)
14 are made applicable to the corporation by the certificate of
15 incorporation.

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17 10. N.J.S.14A:3-6 is repealed.

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19 11. This act shall take effect immediately.

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25 Revises law concerning derivative proceedings and shareholder
class actions.