

Strategies For Single-Member Special Litigation Committees

By **Josh Bloom** (March 1, 2024)

Under Delaware law, derivative claims belong to the company, not stockholders. When faced with a derivative suit, Delaware law allows company boards to form a special litigation committee, or SLC, of independent directors to investigate the claims and determine whether pursuing them is in the company's best interest.

If an SLC determines that the derivative litigation should not proceed, that determination is subject to judicial review.[1]

On Feb. 1, the Delaware Supreme Court issued a brief but notable order in *In re: Baker Hughes, a GE Company, Derivative Litigation*. [2] Baker Hughes arose from a series of 2018 transactions between Baker Hughes Co. and General Electric Co., its then-controlling stockholder.

GE was facing liquidity issues, and wanted to address those issues by modifying its relationship with Baker Hughes — including selling down its Baker Hughes stake. [3] But GE needed Baker Hughes' consent to do so.

After months of negotiations, Baker Hughes agreed to allow GE to sell some of its Baker Hughes shares. [4] Baker Hughes and GE also agreed to modify various commercial contracts between them, or their affiliates, through which GE provided services and products to Baker Hughes. [5]

Some of Baker Hughes' minority stockholders brought a derivative suit claiming these were unfair, conflicted transactions. [6] Those claims survived a motion to dismiss, prompting Baker Hughes to form an SLC to determine whether pursuing the claims was in the company's best interest.

After a 12-month investigation, the SLC determined it was not, and moved to dismiss them. The Delaware Chancery Court granted the SLC's motion to dismiss. And the Supreme Court affirmed.

The Supreme Court's order affirming dismissal was notable in two respects. First, the order upheld the Court of Chancery allowing and considering live testimony from the committee during argument on the committee's motion to dismiss. [7] While special litigation committee members are frequently deposed, such live testimony from a committee member at argument is rare, if not unprecedented.

Second, and perhaps of greater note, the Baker Hughes SLC had a single member. [8] Baker Hughes is at least the third recent example of a well-known public company using a single-member SLC. [9] That is significant because the Court of Chancery has described single-member SLCs as "not ideal." [10]

Indeed, single-member SLCs are subject to heightened scrutiny compared to committees with multiple members. While all SLCs must demonstrate their independence, a single-member committee may need to go a step further, because — as the Court of Chancery said in 1985 in *Lewis v. Fuqua* — it "should, like Caesar's wife, be above reproach." [11]



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Single-member SLCs thus present unique challenges. But they also provide unique opportunities. When working with single-member SLCs, there are several strategies counsel should employ to maximize the chances that the committee will execute its mandate successfully.

Take advantage of the reduced scheduling burden of a single-member SLC.

One basic but important benefit of a single-member SLC is the relative ease and flexibility of scheduling.

Corporate directors are busy people, often with numerous commitments beyond their directorships. When multiple directors comprise an SLC, scheduling — be it committee meetings, witness interviews, or anything else — can be a significant logistical obstacle. The obstacle becomes even greater when plans need to change at the last minute.

Having a single-member SLC affords a relatively high degree of freedom and flexibility when it comes to scheduling. Counsel should leverage that to the greatest extent possible.

That includes scheduling witness interviews in the order most helpful for the investigation, rather than based on when it happens to be convenient for multiple committee members. That also includes having frequent calls or meetings with the SLC on at least a weekly basis to discuss the investigation's status.

And it includes setting up a process or mechanism with the SLC to obtain expedited approvals as appropriate, to keep the investigation on track.

Make early and strategic use of experts.

There is a good chance that a single-member SLC will not have a deep background in the area or areas being investigated. Corporate boards are increasingly composed of individuals with largely complementary, rather than overlapping, skillsets.

So an SLC member who was elected to the board to provide expertise in a particular geography or technology may be less facile with a complicated regulatory or financial issue underlying the derivative claims at issue.

Effective use of experts can mitigate a single-member SLC's initial lack of proficiency in at least two different ways. First, experts can assist the SLC by preparing a report or other work product on a key issue, such as the valuation of a transaction.

In addition to educating the SLC through its work product, the expert can also help the SLC focus its investigation more broadly, by explaining to the SLC what information is needed and suggesting avenues for obtaining that information.

Second, experts can help to serve as a sounding board for the SLC. One potential drawback of a committee of one is less opportunity for debate and deliberation. An expert can potentially mitigate that issue by serving as an intellectual sparring partner for a single-member SLC.

That is particularly true if the SLC is willing and able to retain an expert separate and apart from any experts preparing work product. Such an expert could review the facts developed and any reports prepared, and provide an objective perspective for the SLC to consider.

Depending on the stage of the investigation, such an expert could also be brought in deliberately to play a devil's advocate role, to stress test the SLC's reasoning and improve its decision making.

Ensure the SLC member is particularly active in the investigation.

It is always important for SLC members to take an active role in their investigation. But it is particularly important — indeed, necessary — when the SLC is composed of a sole member.

While an SLC can, and should, delegate certain tasks to its advisers, the SLC, not its advisers, ultimately is responsible for recommending what the company should do with the claims it is investigating.

In making that recommendation, it is important that the SLC, among other things, understands the documentary record, ensures its questions for key witnesses are asked and answered to its satisfaction, and has a view on key witnesses' credibility.

In the single-member SLC context, those responsibilities cannot be shared or divided. Accordingly, a single-member SLC and its counsel should constantly consider throughout the investigation what the key evidence is, and who the most important witnesses are.

Counsel should then ensure the SLC has ready access to those materials, and participates in all interviews or substantive interactions with key individuals.

That approach will not only bolster the quality of the sole-member SLC's investigation, but can also give the SLC more options to address potential challenges to its investigation down the line. For example, as in Baker Hughes, the more actively involved a single-member SLC is in an investigation, the more viable an option it may be to offer that member's live testimony to support the SLC's conclusions.

Avoid communications with other board members about the investigation.

Sole-member SLCs also need to be particularly cautious about their communications with fellow board members regarding the investigation. An SLC that prejudices the outcome of its investigation is vulnerable to challenge.[12]

Because a single-member SLC is a committee of one, anything the member says about the investigation while it is ongoing can easily be misinterpreted as the SLC's final, definitive position — even if that is not the case.

It may be tempting — indeed, more efficient in many instances — for a single-member SLC to provide informal updates or make requests during her or his normal course discussions with colleagues. But given that sole-member SLCs can be subject to heightened scrutiny, the SLC should avoid saying anything about the investigation to the greatest extent possible.

And if something must be said about the investigation, the SLC should endeavor to only communicate about the investigation through, and with input from, its independent counsel.

Single-member SLCs also need to be cognizant of how others could perceive their general interactions with fellow board members outside of the formal board setting. Single-member SLCs should be particularly cautious when it comes to giving or receiving anything from the subjects of the investigation.

That includes gifts the subjects of the investigation may send to a wide range of people — think a widely-distributed holiday gift — of whom the SLC just happens to be one.

Be thoughtful about potentially adding a new member.

Finally, during the course of the investigation, opportunities may arise to add committee members. For example, the election of new directors at an annual meeting or appointment of a replacement for a resigned director will expand the pool of potential committee members.

Single-member SLCs and their advisers should carefully examine these opportunities to expand the committee. Single-member SLCs are perfectly capable of discharging their responsibilities. But all things being equal, a committee with multiple members is preferable to a committee of one.

Adding members means more perspectives, more opportunities to engage in deliberation, and the ability to divide work. It also means eliminating the heightened scrutiny applicable to single-member SLCs.

However, adding a new member mid-investigation raises its own concerns. One concern is maintaining independence.

The bar for independence in the SLC context can be higher than it is in other contexts. For example, an "independent" director under stock exchange listing rules is not necessarily "independent" under Delaware law for SLC purposes.

Determining whether a new director is sufficiently independent to join the SLC can require a fairly deep dive into the potential addition's background. Single-member SLCs and their advisers should begin diligence as soon as possible on potential additions.

One way to do so is by providing potential members a questionnaire about their relationships with others involved in the investigation. If that diligence reveals problematic connections, the SLC will likely need to avoid adding that new director.

The second concern is in regard to the new member's or members' ability to adequately get up to speed and meaningfully contribute to the SLC process in time. One important benefit of an SLC investigation is that discovery in the underlying derivative action is usually stayed during that time. That can be a substantial resource saver for a company.

But absent unusual circumstances, the stays are not indefinite. Thus, as a practical matter, an SLC often has a fixed window — i.e., the duration of the stay — to complete its investigation.[13]

In every investigation there will come a point when adding an additional member no longer makes sense. Perhaps the stay is set to expire in relatively short order, and it is simply not possible for someone new to come in, evaluate what has been done and make an informed decision in time.

Or perhaps all the main witness interviews have already happened, and there is not time to revisit them. Under those circumstances, there may be little actual benefit — and a court may give little credit — to adding an additional member who plays no role in shaping the investigation.

In that case, adding a new member can ultimately do more harm than good to the integrity of the SLC's investigation.

Conclusion

Baker Hughes is important confirmation that, even if not ideal, single-member SLCs are legitimate and effective when utilized properly. A company that believes that it is in its and its stockholders' best interests to form an SLC to investigate derivative claims should not dismiss that path out of hand, merely because it can only form a one-member SLC.

With thought and planning, steps can be taken to maximize the benefits and mitigate the risks that accompany sole-member SLCs.

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[1] See generally *Zapata Corp. v. Maldonado*, 430 A.2d 779, 785 (Del. 1981) (creating two step analysis to evaluate challenges to an SLC dismissal recommendation).

[2] *In re: Baker Hughes*, No. 169, 2023, 2024 WL 371962 (Del. Feb. 1, 2024).

[3] *In re: Baker Hughes, a GE Co., Derivative Litig.*, No. 2019-0201-LWW, 2023 WL 2967780, at *2-*7 (Del. Ch. Apr. 17, 2023).

[4] *Id.*

[5] *Id.*

[6] *Id.*

[7] *In re Baker Hughes*, No. 169, 2023, 2024 WL 371962 at *1.

[8] *Id.*

[9] See, e.g., *Teamsters Loc. 443 Health Servs. & Ins. Plan v. Chou*, No. 2019-0816-SG, 2023 WL 7986729 (Del. Ch. Nov. 17, 2023); *Orlando Police Pension Fund v. Dorsey*, No. 2021-0041-JTL (Del. Ch.).

[10] *In re: Baker Hughes*, No. 2019-0201-LWW, 2023 WL 2967780, at *1 (Del. Ch. Apr. 17, 2023).

[11] *Lewis v. Fuqua*, 502 A.2d 962, 967 (Del. Ch. 1985).

[12] See, e.g., *Biondi v. Scrushy*, 820 A.2d 1148, 1165-1166 (Del. Ch. 2003) (denying SLC's motion to stay where SLC chairman expressed view on investigation outcome "when the SLC's own investigation was just getting underway.").

[13] SLCs can seek, and often receive, one extension of the stay if needed. But extension requests are subject to challenge, are not guaranteed, and are usually not indefinite.