

1-1 By: Martinez Fischer (Senate Sponsor - Hancock) H.B. No. 3603
 1-2 (In the Senate - Received from the House May 7, 2019;
 1-3 May 14, 2019, read first time and referred to Committee on Business
 1-4 & Commerce; May 20, 2019, reported favorably by the following vote:
 1-5 Yeas 8, Nays 0; May 20, 2019, sent to printer.)

1-6 COMMITTEE VOTE

	Yea	Nay	Absent	PNV
1-7 Hancock	X			
1-8 Nichols	X			
1-9 Campbell	X			
1-10 Creighton			X	
1-11 Menéndez	X			
1-12 Paxton	X			
1-13 Schwertner	X			
1-14 Whitmire	X			
1-15 Zaffirini	X			

1-17 A BILL TO BE ENTITLED
 1-18 AN ACT

1-19 relating to derivative proceedings on behalf of for-profit
 1-20 corporations, limited liability companies, and limited
 1-21 partnerships.

1-22 BE IT ENACTED BY THE LEGISLATURE OF THE STATE OF TEXAS:

1-23 SECTION 1. Section 21.551(2), Business Organizations Code,
 1-24 is amended to read as follows:

1-25 (2) "Shareholder" means a shareholder as defined by
 1-26 Section 1.002 or [includes] a beneficial owner whose shares are
 1-27 held in a voting trust or by a nominee on the beneficial owner's
 1-28 behalf.

1-29 SECTION 2. Section 21.552, Business Organizations Code, is
 1-30 amended to read as follows:

1-31 Sec. 21.552. STANDING TO BRING PROCEEDING. (a) Subject
 1-32 to Subsection (b), a [A] shareholder may not institute or maintain a
 1-33 derivative proceeding unless:

1-34 (1) the shareholder:

1-35 (A) was a shareholder of the corporation at the
 1-36 time of the act or omission complained of; or

1-37 (B) became a shareholder by operation of law
 1-38 originating from a person that was a shareholder at the time of the
 1-39 act or omission complained of; and

1-40 (2) the shareholder fairly and adequately represents
 1-41 the interests of the corporation in enforcing the right of the
 1-42 corporation.

1-43 (b) If the converted entity in a conversion is a
 1-44 corporation, a shareholder of that corporation may not institute or
 1-45 maintain a derivative proceeding based on an act or omission that
 1-46 occurred with respect to the converting entity before the date of
 1-47 the conversion unless:

1-48 (1) the shareholder was an equity owner of the
 1-49 converting entity at the time of the act or omission; and

1-50 (2) the shareholder fairly and adequately represents
 1-51 the interests of the corporation in enforcing the right of the
 1-52 corporation.

1-53 SECTION 3. Section 21.553(b), Business Organizations Code,
 1-54 is amended to read as follows:

1-55 (b) The waiting period required by Subsection (a) before a
 1-56 derivative proceeding may be instituted is not required or, if
 1-57 applicable, shall terminate if:

1-58 (1) the shareholder has been [~~previously~~] notified
 1-59 that the demand has been rejected by the corporation;

1-60 (2) the corporation is suffering irreparable injury;

1-61 or

2-1 (3) irreparable injury to the corporation would result
2-2 by waiting for the expiration of the 90-day period.

2-3 SECTION 4. Section 21.554, Business Organizations Code, is
2-4 amended to read as follows:

2-5 Sec. 21.554. DETERMINATION BY DIRECTORS OR INDEPENDENT
2-6 PERSONS. (a) A determination of how to proceed on allegations made
2-7 in a demand or petition relating to a derivative proceeding must be
2-8 made by an affirmative vote of the majority of:

2-9 (1) all ~~the~~ independent and disinterested directors
2-10 of the corporation, regardless of whether ~~present at a meeting of~~
2-11 ~~the board of directors of the corporation at which interested~~
2-12 ~~directors are not present at the time of the vote if~~ the
2-13 independent and disinterested directors constitute a quorum of the
2-14 board of directors;

2-15 (2) a committee consisting of one ~~two~~ or more
2-16 independent and disinterested directors appointed by an
2-17 affirmative vote of the majority of one or more independent and
2-18 disinterested directors ~~present at a meeting of the board of~~
2-19 ~~directors~~, regardless of whether the independent and
2-20 disinterested directors constitute a quorum of the board of
2-21 directors; or

2-22 (3) a panel of one or more independent and
2-23 disinterested individuals ~~persons~~ appointed by the court on a
2-24 motion by the corporation listing the names of the individuals
2-25 ~~persons~~ to be appointed and stating that, to the best of the
2-26 corporation's knowledge, the individuals ~~persons~~ to be appointed
2-27 are disinterested and qualified to make the determinations
2-28 contemplated by Section 21.558.

2-29 (b) The court shall appoint a panel under Subsection (a)(3)
2-30 if the court finds that the individuals ~~persons~~ recommended by
2-31 the corporation are independent and disinterested and are otherwise
2-32 qualified with respect to expertise, experience, independent
2-33 judgment, and other factors considered appropriate by the court
2-34 under the circumstances to make the determinations. An individual
2-35 ~~A person~~ appointed by the court to a panel under this section may
2-36 not be held liable to the corporation or the corporation's
2-37 shareholders for an action taken or omission made by the individual
2-38 ~~person~~ in that capacity, except for an act or omission
2-39 constituting fraud or wilful misconduct.

2-40 SECTION 5. Section 21.555, Business Organizations Code, is
2-41 amended to read as follows:

2-42 Sec. 21.555. STAY OF PROCEEDING. (a) If the ~~domestic or~~
2-43 ~~foreign~~ corporation that is the subject of a derivative proceeding
2-44 commences an inquiry into the allegations made in a demand or
2-45 petition and the person or group of persons described by Section
2-46 21.554 is conducting an active review of the allegations in good
2-47 faith, the court shall stay a derivative proceeding for not more
2-48 than 60 days until the review is completed and a determination is
2-49 made by the person or group regarding what further action, if any,
2-50 should be taken.

2-51 (b) To obtain a stay, the ~~domestic or foreign~~ corporation
2-52 must ~~shall~~ provide the court with a written statement agreeing to
2-53 advise the court and the shareholder making the demand of the
2-54 determination promptly on the completion of the review of the
2-55 matter.

2-56 (c) A stay, on motion ~~application~~, may be reviewed every
2-57 60 days for continuation ~~the continued necessity~~ of the stay if
2-58 the corporation provides the court and the shareholder with a
2-59 written statement of the status of the review and the reasons why an
2-60 extension for a period not to exceed 60 additional days is
2-61 appropriate. An extension shall be granted for a period not to
2-62 exceed 60 days if the court determines that the continuation is
2-63 appropriate in the interests of the corporation.

2-64 ~~[(c) If the review and determination made by the person or~~
2-65 ~~group is not completed before the 61st day after the stay is ordered~~
2-66 ~~by the court, the stay may be renewed for one or more additional~~
2-67 ~~60-day periods if the domestic or foreign corporation provides the~~
2-68 ~~court and the shareholder with a written statement of the status of~~
2-69 ~~the review and the reasons why a continued extension of the stay is~~

3-1 ~~necessary.]~~

3-2 SECTION 6. Section 21.556, Business Organizations Code, is
3-3 amended to read as follows:

3-4 Sec. 21.556. DISCOVERY. (a) If a ~~[domestic or foreign]~~
3-5 corporation proposes to dismiss a derivative proceeding under
3-6 Section 21.558, discovery by a shareholder after the filing of the
3-7 derivative proceeding in accordance with this subchapter shall be
3-8 limited to:

3-9 (1) facts relating to whether the person or ~~[group of]~~
3-10 persons described by Section 21.554 are ~~[21.558 is]~~ independent and
3-11 disinterested;

3-12 (2) the good faith of the inquiry and review by the
3-13 person or group; and

3-14 (3) the reasonableness of the procedures followed by
3-15 the person or group in conducting the review.

3-16 (b) Discovery described by Subsection (a) may not be
3-17 expanded to include a fact or substantive matter regarding the act,
3-18 omission, or other matter that is the subject matter of the
3-19 derivative proceeding but the scope of discovery shall not be so
3-20 limited ~~[. The scope of discovery may be expanded]~~ if the court
3-21 determines after notice and hearing that a good faith review of the
3-22 allegations ~~[for purposes of Section 21.558]~~ has not been made by an
3-23 independent and disinterested person or group in accordance with
3-24 Sections 21.554 and 21.558 ~~[that section]~~.

3-25 SECTION 7. Section 21.557, Business Organizations Code, is
3-26 amended to read as follows:

3-27 Sec. 21.557. TOLLING OF STATUTE OF LIMITATIONS. A written
3-28 demand filed with the corporation under Section 21.553 tolls the
3-29 statute of limitations on the claim on which demand is made until
3-30 the later ~~[earlier]~~ of:

3-31 (1) the 31st ~~[91st]~~ day after the expiration of any
3-32 waiting period under Section 21.553 ~~[date of the demand]~~; or

3-33 (2) the 31st day after the expiration of any stay
3-34 granted under Section 21.555, including all continuations of the
3-35 stay ~~[date the corporation advises the shareholder that the demand~~
3-36 ~~has been rejected or the review has been completed]~~.

3-37 SECTION 8. Section 21.558, Business Organizations Code, is
3-38 amended to read as follows:

3-39 Sec. 21.558. DISMISSAL OF DERIVATIVE PROCEEDING. (a) A
3-40 court, sitting in equity as the finder of fact, shall dismiss a
3-41 derivative proceeding on a motion by the corporation if the person
3-42 or group of persons described by Section 21.554 determines in good
3-43 faith, after conducting a reasonable inquiry and based on factors
3-44 the person or group considers appropriate under the circumstances,
3-45 that continuation of the derivative proceeding is not in the best
3-46 interests of the corporation.

3-47 (b) In determining whether the requirements of Subsection
3-48 (a) have been met, the burden of proof shall be on:

3-49 (1) the plaintiff shareholder if:

3-50 (A) the majority of the board of directors
3-51 consists of independent and disinterested directors at the time the
3-52 determination is made;

3-53 (B) the determination is made by a panel of one or
3-54 more independent and disinterested persons appointed under Section
3-55 21.554(a)(3); or

3-56 (C) the corporation presents prima facie
3-57 evidence that demonstrates that the applicable person or persons
3-58 making the determination ~~[directors appointed]~~ under Section
3-59 21.554(a) ~~[21.554(a)(2)]~~ are independent and disinterested; or

3-60 (2) the corporation in any other circumstance.

3-61 SECTION 9. Section 21.559, Business Organizations Code, is
3-62 amended to read as follows:

3-63 Sec. 21.559. ALLEGATIONS ~~[PROCEEDING INSTITUTED]~~ AFTER
3-64 DEMAND REJECTED. If a derivative proceeding is instituted after a
3-65 demand is rejected, the petition must allege with particularity
3-66 facts that establish that the rejection was not made in accordance
3-67 with the requirements and standards under ~~[of]~~ Sections 21.554 and
3-68 21.558.

3-69 SECTION 10. Section 21.561, Business Organizations Code, is

4-1 amended to read as follows:

4-2 Sec. 21.561. PAYMENT OF EXPENSES. (a) In this section,
4-3 "expenses" means reasonable expenses incurred by a party in a
4-4 derivative proceeding, including:

4-5 (1) attorney's fees;

4-6 (2) costs in pursuing an investigation of the matter
4-7 that was the subject of the derivative proceeding; or

4-8 (3) expenses for which the [~~domestic or foreign~~]
4-9 corporation [~~or a corporate defendant~~] may be required to indemnify
4-10 another person.

4-11 (b) On termination of a derivative proceeding, the court may
4-12 order:

4-13 (1) the [~~domestic or foreign~~] corporation to pay [~~the~~]
4-14 expenses the plaintiff incurred in the proceeding if the court
4-15 finds the proceeding has resulted in a substantial benefit to the
4-16 [~~domestic or foreign~~] corporation;

4-17 (2) the plaintiff to pay [~~the~~] expenses the [~~domestic~~
4-18 ~~or foreign~~] corporation or other defendant incurred in
4-19 investigating and defending the proceeding if the court finds the
4-20 proceeding has been instituted or maintained without reasonable
4-21 cause or for an improper purpose; or

4-22 (3) a party to pay [~~the~~] expenses incurred by another
4-23 party relating to the filing of a pleading, motion, or other paper
4-24 if the court finds the pleading, motion, or other paper:

4-25 (A) was not well grounded in fact after
4-26 reasonable inquiry;

4-27 (B) was not warranted by existing law or a good
4-28 faith argument for the application, extension, modification, or
4-29 reversal of existing law; or

4-30 (C) was interposed for an improper purpose, such
4-31 as to harass, cause unnecessary delay, or cause a needless increase
4-32 in the cost of litigation.

4-33 SECTION 11. Section 21.562, Business Organizations Code, is
4-34 amended to read as follows:

4-35 Sec. 21.562. APPLICATION TO FOREIGN CORPORATIONS. (a) In a
4-36 derivative proceeding brought in the right of a foreign
4-37 corporation, the matters covered by this subchapter are governed by
4-38 the laws of the jurisdiction of formation [~~incorporation~~] of the
4-39 foreign corporation, except for Sections 21.555, 21.560, and
4-40 21.561, which are procedural provisions and do not relate to the
4-41 internal affairs of the foreign corporation, unless applying the
4-42 laws of the jurisdiction of formation of the foreign corporation
4-43 requires otherwise with respect to Section 21.555.

4-44 (b) In the case of matters relating to a foreign corporation
4-45 under Section 21.555 [~~21.554~~], a reference to a person or group of
4-46 persons described by Section 21.554 [~~that section~~] refers to a
4-47 person or group entitled under the laws of the jurisdiction of
4-48 formation [~~incorporation~~] of the foreign corporation to make the
4-49 determination described by Section 21.554(a) [~~review and dispose of~~
4-50 ~~a derivative proceeding~~]. The standard of review of a
4-51 determination [~~decision~~] made by the person or group [~~to dismiss~~
4-52 ~~the derivative proceeding~~] shall be governed by the laws of the
4-53 jurisdiction of formation [~~incorporation~~] of the foreign
4-54 corporation.

4-55 SECTION 12. Section 21.563, Business Organizations Code, is
4-56 amended to read as follows:

4-57 Sec. 21.563. CLOSELY HELD CORPORATION. (a) In this
4-58 section, "closely held corporation" means a corporation that has:

4-59 (1) fewer than 35 shareholders; and

4-60 (2) no shares listed on a national securities exchange
4-61 or regularly quoted in an over-the-counter market by one or more
4-62 members of a national securities association.

4-63 (b) Sections 21.552-21.560 [~~21.552-21.559~~] do not apply to
4-64 a claim or a derivative proceeding by a shareholder of a closely
4-65 held corporation against a director, officer, or shareholder of the
4-66 corporation. In the event the claim or derivative proceeding is
4-67 also made against a person who is not that director, officer, or
4-68 shareholder, this subsection applies only to the claim or
4-69 derivative proceeding against the director, officer, or

5-1 shareholder.

5-2 (c) If Sections 21.552-21.560 do not apply because of
5-3 Subsection (b) and if justice requires:

5-4 (1) a derivative proceeding brought by a shareholder
5-5 of a closely held corporation may be treated by a court as a direct
5-6 action brought by the shareholder for the shareholder's own
5-7 benefit; and

5-8 (2) a recovery in a direct or derivative proceeding by
5-9 a shareholder may be paid directly to the plaintiff or to the
5-10 corporation if necessary to protect the interests of creditors or
5-11 other shareholders of the corporation.

5-12 (d) Other provisions of state law govern whether a
5-13 shareholder has a direct cause of action or right to sue a director,
5-14 officer, or shareholder, and this section may not be construed to
5-15 create that direct cause of action or right to sue.

5-16 SECTION 13. Section 101.451, Business Organizations Code,
5-17 is amended by amending Subdivision (2) and adding Subdivision (3)
5-18 to read as follows:

5-19 (2) "Managing entity" means an entity that is either:
5-20 (A) a manager of a limited liability company that
5-21 is managed by managers; or

5-22 (B) a member of a limited liability company that
5-23 is managed by members who are entitled to manage the company.

5-24 (3) "Member" means [~~includes~~] a person who is a member
5-25 or is an assignee of a membership interest or a person who
5-26 beneficially owns a membership interest through a voting trust or a
5-27 nominee on the person's behalf.

5-28 SECTION 14. Section 101.452, Business Organizations Code,
5-29 is amended to read as follows:

5-30 Sec. 101.452. STANDING TO BRING PROCEEDING. (a) Subject
5-31 to Subsection (b), a [A] member may not institute or maintain a
5-32 derivative proceeding unless:

5-33 (1) the member:

5-34 (A) was a member of the limited liability company
5-35 at the time of the act or omission complained of; or

5-36 (B) became a member by operation of law
5-37 originating from a person that was a member at the time of the act or
5-38 omission complained of; and

5-39 (2) the member fairly and adequately represents the
5-40 interests of the limited liability company in enforcing the right
5-41 of the limited liability company.

5-42 (b) If the converted entity in a conversion is a limited
5-43 liability company, a member of that limited liability company may
5-44 not institute or maintain a derivative proceeding based on an act or
5-45 omission that occurred with respect to the converting entity before
5-46 the date of the conversion unless:

5-47 (1) the member was an equity owner of the converting
5-48 entity at the time of the act or omission; and

5-49 (2) the member fairly and adequately represents the
5-50 interests of the limited liability company in enforcing the right
5-51 of the limited liability company.

5-52 SECTION 15. Section 101.453(b), Business Organizations
5-53 Code, is amended to read as follows:

5-54 (b) The waiting period required by Subsection (a) before a
5-55 derivative proceeding may be instituted is not required or, if
5-56 applicable, shall terminate if:

5-57 (1) the member has been [~~previously~~] notified that the
5-58 demand has been rejected by the limited liability company;

5-59 (2) the limited liability company is suffering
5-60 irreparable injury; or

5-61 (3) irreparable injury to the limited liability
5-62 company would result by waiting for the expiration of the 90-day
5-63 period.

5-64 SECTION 16. Section 101.454, Business Organizations Code,
5-65 is amended to read as follows:

5-66 Sec. 101.454. DETERMINATION BY GOVERNING OR INDEPENDENT
5-67 PERSONS. (a) The determination of how to proceed on allegations
5-68 made in a demand or petition relating to a derivative proceeding
5-69 must be made by an affirmative vote of the majority of:

6-1 (1) the independent and disinterested governing
 6-2 persons of the limited liability company, whether one or more, even
 6-3 if the independent and disinterested governing persons are not a
 6-4 majority of the governing persons of the limited liability company
 6-5 ~~[present at a meeting of the governing authority at which~~
 6-6 ~~interested governing persons are not present at the time of the vote~~
 6-7 ~~if the independent and disinterested governing persons constitute a~~
 6-8 ~~quorum of the governing authority];~~

6-9 (2) a committee consisting of one ~~[two]~~ or more
 6-10 independent and disinterested governing persons appointed by the
 6-11 majority of one or more independent and disinterested governing
 6-12 persons of the limited liability company, even if the appointing
 6-13 independent and disinterested governing persons are not a majority
 6-14 of the governing persons of the limited liability company ~~[present~~
 6-15 ~~at a meeting of the governing authority, regardless of whether the~~
 6-16 ~~independent and disinterested governing persons constitute a~~
 6-17 ~~quorum of the governing authority]; or~~

6-18 (3) a panel of one or more independent and
 6-19 disinterested individuals ~~[persons]~~ appointed by the court on a
 6-20 motion by the limited liability company listing the names of the
 6-21 individuals ~~[persons]~~ to be appointed and stating that, to the best
 6-22 of the limited liability company's knowledge, the individuals
 6-23 ~~[persons]~~ to be appointed are disinterested and qualified to make
 6-24 the determinations contemplated by Section 101.458.

6-25 (b) An entity to which this subsection applies is
 6-26 independent and disinterested under this section only if its
 6-27 decision with respect to the limited liability company's derivative
 6-28 proceeding is made by a majority of its governing persons who are
 6-29 independent and disinterested with respect to that derivative
 6-30 proceeding, even if those governing persons are not a majority of
 6-31 its governing persons. This subsection applies to an entity that
 6-32 is:

6-33 (1) a managing entity of the limited liability
 6-34 company; or
 6-35 (2) directly, or indirectly through one or more other
 6-36 entities, a governing person of that managing entity.

6-37 (c) The court shall appoint a panel under Subsection (a)(3)
 6-38 if the court finds that the individuals ~~[persons]~~ recommended by
 6-39 the limited liability company are independent and disinterested and
 6-40 are otherwise qualified with respect to expertise, experience,
 6-41 independent judgment, and other factors considered appropriate by
 6-42 the court under the circumstances to make the determinations. An
 6-43 individual ~~[A person]~~ appointed by the court to a panel under this
 6-44 section may not be held liable to the limited liability company or
 6-45 the limited liability company's members for an action taken or
 6-46 omission made by the individual ~~[person]~~ in that capacity, except
 6-47 for acts or omissions constituting fraud or wilful misconduct.

6-48 SECTION 17. Section 101.455, Business Organizations Code,
 6-49 is amended to read as follows:

6-50 Sec. 101.455. STAY OF PROCEEDING. (a) If the ~~[domestic or~~
 6-51 ~~foreign]~~ limited liability company that is the subject of a
 6-52 derivative proceeding commences an inquiry into the allegations
 6-53 made in a demand or petition and the person or group of persons
 6-54 described by Section 101.454 is conducting an active review of the
 6-55 allegations in good faith, the court shall stay a derivative
 6-56 proceeding for not more than 60 days until the review is completed
 6-57 and a determination is made by the person or group regarding what
 6-58 further action, if any, should be taken.

6-59 (b) To obtain a stay, the ~~[domestic or foreign]~~ limited
 6-60 liability company must ~~[shall]~~ provide the court with a written
 6-61 statement agreeing to advise the court and the member making the
 6-62 demand of the determination promptly on the completion of the
 6-63 review of the matter.

6-64 (c) A stay, on motion, may be reviewed every 60 days for
 6-65 continuation ~~[the continued necessity]~~ of the stay if the limited
 6-66 liability company provides the court and the member with a written
 6-67 statement of the status of the review and the reasons why an
 6-68 extension for a period not to exceed 60 additional days is
 6-69 appropriate. An extension shall be granted for a period not to

7-1 exceed 60 days if the court determines that the continuation is
7-2 appropriate in the interests of the limited liability company.

7-3 ~~[(c) If the review and determination made by the person or
7-4 group is not completed before the 61st day after the date on which
7-5 the court orders the stay, the stay may be renewed for one or more
7-6 additional 60-day periods if the domestic or foreign limited
7-7 liability company provides the court and the member with a written
7-8 statement of the status of the review and the reasons why a
7-9 continued extension of the stay is necessary.]~~

7-10 SECTION 18. Section 101.456, Business Organizations Code,
7-11 is amended to read as follows:

7-12 Sec. 101.456. DISCOVERY. (a) If a ~~[domestic or foreign]~~
7-13 limited liability company proposes to dismiss a derivative
7-14 proceeding under Section 101.458, discovery by a member after the
7-15 filing of the derivative proceeding in accordance with this
7-16 subchapter shall be limited to:

7-17 (1) facts relating to whether the person or ~~[group of]~~
7-18 persons described by Section 101.454 are ~~[101.458 is]~~ independent
7-19 and disinterested;

7-20 (2) the good faith of the inquiry and review by the
7-21 person or group; and

7-22 (3) the reasonableness of the procedures followed by
7-23 the person or group in conducting the review.

7-24 (b) Discovery described by Subsection (a) may not be
7-25 expanded to include a fact or substantive matter regarding the act,
7-26 omission, or other matter that is the subject matter of the
7-27 derivative proceeding but the scope of discovery shall not be so
7-28 limited ~~[-. The scope of discovery may be expanded]~~ if the court
7-29 determines after notice and hearing that a good faith review of the
7-30 allegations ~~[for purposes of Section 101.458]~~ has not been made by
7-31 an independent and disinterested person or group in accordance with
7-32 Sections 101.454 and 101.458 ~~[that section]~~.

7-33 SECTION 19. Section 101.457, Business Organizations Code,
7-34 is amended to read as follows:

7-35 Sec. 101.457. TOLLING OF STATUTE OF LIMITATIONS. A written
7-36 demand filed with the limited liability company under Section
7-37 101.453 tolls the statute of limitations on the claim on which
7-38 demand is made until the later ~~[earlier]~~ of:

7-39 (1) the 31st ~~[91st]~~ day after the expiration of any
7-40 waiting period under Section 153.403 ~~[date of the demand]~~; or

7-41 (2) the 31st day after the expiration of any stay
7-42 granted under Section 153.405, including all continuations of the
7-43 stay ~~[date the limited liability company advises the member that~~
7-44 ~~the demand has been rejected or the review has been completed]~~.

7-45 SECTION 20. Section 101.458, Business Organizations Code,
7-46 is amended to read as follows:

7-47 Sec. 101.458. DISMISSAL OF DERIVATIVE PROCEEDING. (a) A
7-48 court, sitting in equity as the finder of fact, shall dismiss a
7-49 derivative proceeding on a motion by the limited liability company
7-50 if the person or group of persons described by Section 101.454
7-51 determines in good faith, after conducting a reasonable inquiry and
7-52 based on factors the person or group considers appropriate under
7-53 the circumstances, that continuation of the derivative proceeding
7-54 is not in the best interests of the limited liability company.

7-55 (b) In determining whether the requirements of Subsection
7-56 (a) have been met, the burden of proof shall be on:

7-57 (1) the plaintiff member if:

7-58 (A) the applicable person or persons making the
7-59 determination under Section 101.454(a)(1) or (2) are ~~[majority of~~
7-60 ~~the governing authority consists of]~~ independent and disinterested
7-61 ~~[persons]~~ at the time the determination is made;

7-62 (B) the determination is made by a panel of one or
7-63 more independent and disinterested persons appointed under Section
7-64 101.454(a)(3); or

7-65 (C) the limited liability company presents prima
7-66 facie evidence that demonstrates that the applicable person or
7-67 persons making the determination ~~[appointed]~~ under Section
7-68 101.454(a) ~~[101.454(a)(2)]~~ are independent and disinterested; or

7-69 (2) the limited liability company in any other

8-1 circumstance.

8-2 SECTION 21. Section 101.459, Business Organizations Code,
8-3 is amended to read as follows:

8-4 Sec. 101.459. ALLEGATIONS AFTER ~~[IF]~~ DEMAND REJECTED. If a
8-5 derivative proceeding is instituted after a demand is rejected, the
8-6 petition must allege with particularity facts that establish that
8-7 the rejection was not made in accordance with the requirements and
8-8 standards under ~~[of]~~ Sections 101.454 and 101.458.

8-9 SECTION 22. Section 101.461, Business Organizations Code,
8-10 is amended to read as follows:

8-11 Sec. 101.461. PAYMENT OF EXPENSES. (a) In this section,
8-12 "expenses" means reasonable expenses incurred by a party in a
8-13 derivative proceeding, including:

8-14 (1) attorney's fees;
8-15 (2) costs in ~~[of]~~ pursuing an investigation of the
8-16 matter that was the subject of the derivative proceeding; or
8-17 (3) expenses for which the ~~[domestic or foreign]~~
8-18 limited liability company may be required to indemnify another
8-19 person.

8-20 (b) On termination of a derivative proceeding, the court may
8-21 order:

8-22 (1) the ~~[domestic or foreign]~~ limited liability
8-23 company to pay ~~[the]~~ expenses the plaintiff incurred in the
8-24 proceeding if the court finds the proceeding has resulted in a
8-25 substantial benefit to the ~~[domestic or foreign]~~ limited liability
8-26 company;

8-27 (2) the plaintiff to pay ~~[the]~~ expenses the ~~[domestic
8-28 or foreign]~~ limited liability company or other defendant incurred
8-29 in investigating and defending the proceeding if the court finds
8-30 the proceeding has been instituted or maintained without reasonable
8-31 cause or for an improper purpose; or

8-32 (3) a party to pay ~~[the]~~ expenses incurred by another
8-33 party relating to the filing of a pleading, motion, or other paper
8-34 if the court finds the pleading, motion, or other paper:

8-35 (A) was not well grounded in fact after
8-36 reasonable inquiry;

8-37 (B) was not warranted by existing law or a good
8-38 faith argument for the application, extension, modification, or
8-39 reversal of existing law; or

8-40 (C) was interposed for an improper purpose, such
8-41 as to harass, cause unnecessary delay, or cause a needless increase
8-42 in the cost of litigation.

8-43 SECTION 23. Section 101.462, Business Organizations Code,
8-44 is amended to read as follows:

8-45 Sec. 101.462. APPLICATION TO FOREIGN LIMITED LIABILITY
8-46 COMPANIES. (a) In a derivative proceeding brought in the right of
8-47 a foreign limited liability company, the matters covered by this
8-48 subchapter are governed by the laws of the jurisdiction of
8-49 formation ~~[organization]~~ of the foreign limited liability company,
8-50 except for Sections 101.455, 101.460, and 101.461, which are
8-51 procedural provisions and do not relate to the internal affairs of
8-52 the foreign limited liability company, unless applying the laws of
8-53 the jurisdiction of formation of the foreign limited liability
8-54 company requires otherwise with respect to Section 101.455.

8-55 (b) In the case of matters relating to a foreign limited
8-56 liability company under Section 101.455 ~~[101.454]~~, a reference to a
8-57 person or group of persons described by Section 101.454 ~~[that~~
8-58 ~~section]~~ refers to a person or group entitled under the laws of the
8-59 jurisdiction of formation ~~[organization]~~ of the foreign limited
8-60 liability company to make the determination described by Section
8-61 101.454(a) ~~[review and dispose of a derivative proceeding]~~. The
8-62 standard of review of a determination ~~[decision]~~ made by the person
8-63 or group ~~[to dismiss the derivative proceeding]~~ shall be governed
8-64 by the laws of the jurisdiction of formation ~~[organization]~~ of the
8-65 foreign limited liability company.

8-66 SECTION 24. Section 101.463, Business Organizations Code,
8-67 is amended to read as follows:

8-68 Sec. 101.463. CLOSELY HELD LIMITED LIABILITY COMPANY. (a)
8-69 In this section, "closely held limited liability company" means a

9-1 limited liability company that has:

9-2 (1) fewer than 35 members; and

9-3 (2) no membership interests listed on a national
9-4 securities exchange or regularly quoted in an over-the-counter
9-5 market by one or more members of a national securities association.

9-6 (b) Sections 101.452-101.460 [~~101.452-101.459~~] do not apply
9-7 to a claim or a derivative proceeding by a member of a closely held
9-8 limited liability company against a governing person, member, or
9-9 officer of the limited liability company. In the event the claim or
9-10 derivative proceeding is also made against a person who is not that
9-11 governing person, member, or officer, this subsection applies only
9-12 to the claim or derivative proceeding against the governing person,
9-13 member, or officer.

9-14 (c) If Sections 101.452-101.460 do not apply because of
9-15 Subsection (b) and if justice requires:

9-16 (1) a derivative proceeding brought by a member of a
9-17 closely held limited liability company may be treated by a court as
9-18 a direct action brought by the member for the member's own benefit;
9-19 and

9-20 (2) a recovery in a direct or derivative proceeding by
9-21 a member may be paid directly to the plaintiff or to the limited
9-22 liability company if necessary to protect the interests of
9-23 creditors or other members of the limited liability company.

9-24 (d) Other provisions of state law govern whether a member
9-25 has a direct cause of action or right to sue a governing person,
9-26 member, or officer, and this section may not be construed to create
9-27 that direct cause of action or right to sue.

9-28 SECTION 25. Section 153.401, Business Organizations Code,
9-29 is amended to read as follows:

9-30 Sec. 153.401. DEFINITIONS [~~RIGHT TO BRING ACTION~~]. In this
9-31 subchapter:

9-32 (1) "Derivative proceeding" means a civil suit in the
9-33 right of a domestic limited partnership or, to the extent provided
9-34 by Section 153.412, in the right of a foreign limited partnership.

9-35 (2) "Limited partner" means a person who is a limited
9-36 partner or is an assignee of a partnership interest, including the
9-37 partnership interest of a general partner [~~A limited partner may~~
9-38 ~~bring an action in a court on behalf of the limited partnership to~~
9-39 ~~recover a judgment in the limited partnership's favor if:~~

9-40 [~~(1) all general partners with authority to bring the~~
9-41 ~~action have refused to bring the action; or~~

9-42 [~~(2) an effort to cause those general partners to~~
9-43 ~~bring the action is not likely to succeed].~~

9-44 SECTION 26. Section 153.402, Business Organizations Code,
9-45 is amended to read as follows:

9-46 Sec. 153.402. STANDING TO BRING PROCEEDING [~~PROPER~~
9-47 ~~PLAINTIFF~~]. (a) Subject to Subsection (b), a limited partner may
9-48 not institute or maintain a derivative proceeding unless:

9-49 (1) the limited partner:

9-50 (A) was a limited partner of the limited
9-51 partnership at the time of the act or omission complained of; or

9-52 (B) became a limited partner by operation of law
9-53 originating from a person that was a limited partner or general
9-54 partner at the time of the act or omission complained of; and

9-55 (2) the limited partner fairly and adequately
9-56 represents the interests of the limited partnership in enforcing
9-57 the right of the limited partnership.

9-58 (b) If the converted entity in a conversion is a limited
9-59 partnership, a limited partner of that limited partnership may not
9-60 institute or maintain a derivative proceeding based on an act or
9-61 omission that occurred with respect to the converting entity before
9-62 the date of the conversion unless:

9-63 (1) the limited partner was an equity owner of the
9-64 converting entity at the time of the act or omission; and

9-65 (2) the limited partner fairly and adequately
9-66 represents the interests of the limited partnership in enforcing
9-67 the right of the limited partnership [~~In a derivative action, the~~
9-68 ~~plaintiff must be a limited partner when the action is brought and:~~

9-69 [~~(1) the person must have been a limited partner at the~~

~~time of the transaction that is the subject of the action, or
 [(2) the person's status as a limited partner must have
 arisen by operation of law or under the terms of the partnership
 agreement from a person who was a limited partner at the time of the
 transaction].~~

SECTION 27. Section 153.403, Business Organizations Code, is amended to read as follows:

Sec. 153.403. DEMAND [PLEADING]. (a) A limited partner may not institute a derivative proceeding until the 91st day after the date a written demand is filed with the limited partnership stating with particularity the act, omission, or other matter that is the subject of the claim or challenge and requesting that the limited partnership take suitable action.

(b) The waiting period required by Subsection (a) before a derivative proceeding may be instituted is not required or, if applicable, shall terminate if:

(1) the limited partner has been notified that the demand has been rejected by the limited partnership;

(2) the limited partnership is suffering irreparable injury; or

(3) irreparable injury to the limited partnership would result by waiting for the expiration of the 90-day period [In a derivative action, the complaint must contain with particularity:

(1) the effort, if any, of the plaintiff to secure initiation of the action by a general partner; or

(2) the reasons for not making the effort].

SECTION 28. Section 153.404, Business Organizations Code, is amended to read as follows:

Sec. 153.404. DETERMINATION BY INDEPENDENT PERSONS [SECURITY FOR EXPENSES OF DEFENDANTS]. (a) A determination of how to proceed on allegations made in a demand or petition relating to a derivative proceeding must be made by an affirmative vote of the majority of:

(1) the independent and disinterested general partners of the limited partnership, whether one or more, even if the independent and disinterested general partners are not a majority of the general partners of the limited partnership;

(2) a committee consisting of one or more independent and disinterested general partners appointed by a majority of one or more independent and disinterested general partners of the limited partnership, even if the appointing independent and disinterested general partners are not a majority of the general partners of the limited partnership; or

(3) a panel of one or more independent and disinterested individuals appointed by the court on a motion by the limited partnership listing the names of the individuals to be appointed and stating that, to the best of the limited partnership's knowledge, the individuals to be appointed are disinterested and qualified to make the determinations contemplated by Section 153.408 [In a derivative action, the court may require the plaintiff to give security for the reasonable expenses incurred or expected to be incurred by a defendant in the action, including reasonable attorney's fees].

(b) An entity to which this subsection applies is independent and disinterested under this section only if its decision with respect to the limited partnership's derivative proceeding is made by a majority of its governing persons who are independent and disinterested with respect to that derivative proceeding, even if those governing persons are not a majority of its governing persons. This subsection applies to an entity that is:

(1) a general partner of the limited partnership; or

(2) directly, or indirectly through one or more other entities, a governing person of that general partner [The court may increase or decrease at any time the amount of the security on a showing that the security provided is inadequate or excessive].

(c) The court shall appoint a panel under Subsection (a)(3) if the court finds that the individuals recommended by the limited partnership are independent and disinterested and are otherwise

11-1 qualified with respect to expertise, experience, independent
 11-2 judgment, and other factors considered appropriate by the court
 11-3 under the circumstances to make the determinations. An individual
 11-4 appointed by the court to a panel under this section may not be held
 11-5 liable to the limited partnership or the limited partnership's
 11-6 partners for an action taken or omission made by the individual in
 11-7 that capacity, except for an act or omission constituting fraud or
 11-8 wilful misconduct [If a plaintiff is unable to give security, the
 11-9 plaintiff may file an affidavit in accordance with the Texas Rules
 11-10 of Civil Procedure].

11-11 ~~[(d) Except as provided by Subsection (c), if a plaintiff~~
 11-12 ~~fails to give the security within a reasonable time set by the~~
 11-13 ~~court, the court shall dismiss the suit without prejudice.~~

11-14 ~~[(e) The court, on final judgment for a defendant and on a~~
 11-15 ~~finding that suit was brought without reasonable cause against the~~
 11-16 ~~defendant, may require the plaintiff to pay reasonable expenses,~~
 11-17 ~~including reasonable attorney's fees, to the defendant, regardless~~
 11-18 ~~of whether security has been required.]~~

11-19 SECTION 29. Section 153.405, Business Organizations Code,
 11-20 is amended to read as follows:

11-21 Sec. 153.405. STAY OF PROCEEDING [EXPENSES OF PLAINTIFF].

11-22 (a) If the limited partnership that is the subject of a derivative
 11-23 proceeding commences an inquiry into the allegations made in a
 11-24 demand or petition and the person or group of persons described by
 11-25 Section 153.404 is conducting an active review of the allegations
 11-26 in good faith, the court shall stay a derivative proceeding for not
 11-27 more than 60 days until the review is completed and a determination
 11-28 is made by the person or group regarding what further action, if
 11-29 any, should be taken.

11-30 (b) To obtain a stay, the limited partnership must provide
 11-31 the court with a written statement agreeing to advise the court and
 11-32 the limited partner making the demand of the determination promptly
 11-33 on the completion of the review of the matter.

11-34 (c) A stay, on motion, may be reviewed every 60 days for
 11-35 continuation of the stay if the limited partnership provides the
 11-36 court and the limited partner with a written statement of the status
 11-37 of the review and the reasons why an extension for a period not to
 11-38 exceed 60 additional days is appropriate. An extension shall be
 11-39 granted for a period not to exceed 60 days if the court determines
 11-40 that the continuation is appropriate in the interests of the
 11-41 partnership [If a derivative action is successful, wholly or
 11-42 partly, or if anything is received by the plaintiff because of a
 11-43 judgment, compromise, or settlement of the action or claim
 11-44 constituting a part of the action, the court may award the plaintiff
 11-45 reasonable expenses, including reasonable attorney's fees, and
 11-46 shall direct the plaintiff to remit to a party identified by the
 11-47 court the remainder of the proceeds received by the plaintiff].

11-48 SECTION 30. Subchapter I, Chapter 153, Business
 11-49 Organizations Code, is amended by adding Sections 153.406, 153.407,
 11-50 153.408, 153.409, 153.410, 153.411, 153.412, and 153.413 to read as
 11-51 follows:

11-52 Sec. 153.406. DISCOVERY. (a) If a limited partnership
 11-53 proposes to dismiss a derivative proceeding under Section 153.408,
 11-54 discovery by a limited partner after the filing of the derivative
 11-55 proceeding in accordance with this subchapter shall be limited to:

11-56 (1) facts relating to whether the person or persons
 11-57 described by Section 153.404 are independent and disinterested;

11-58 (2) the good faith of the inquiry and review by the
 11-59 person or group; and

11-60 (3) the reasonableness of the procedures followed by
 11-61 the person or group in conducting the review.

11-62 (b) Discovery described by Subsection (a) may not be
 11-63 expanded to include a fact or substantive matter regarding the act,
 11-64 omission, or other matter that is the subject matter of the
 11-65 derivative proceeding, but the scope of discovery shall not be so
 11-66 limited if the court determines after notice and hearing that a good
 11-67 faith review of the allegations has not been made by an independent
 11-68 and disinterested person or group in accordance with Sections
 11-69 153.404 and 153.408.

12-1 Sec. 153.407. TOLLING OF STATUTE OF LIMITATIONS. A written
 12-2 demand filed with the limited partnership under Section 153.403
 12-3 tolls the statute of limitations on the claim on which demand is
 12-4 made until the later of:

12-5 (1) the 31st day after the expiration of any waiting
 12-6 period under Section 153.403; or

12-7 (2) the 31st day after the expiration of any stay
 12-8 granted under Section 153.405, including all continuations of the
 12-9 stay.

12-10 Sec. 153.408. DISMISSAL OF DERIVATIVE PROCEEDING. (a) A
 12-11 court, sitting in equity as the finder of fact, shall dismiss a
 12-12 derivative proceeding on a motion by the limited partnership if the
 12-13 person or group of persons described by Section 153.404 determines
 12-14 in good faith, after conducting a reasonable inquiry and based on
 12-15 factors the person or group considers appropriate under the
 12-16 circumstances, that continuation of the derivative proceeding is
 12-17 not in the best interests of the limited partnership.

12-18 (b) In determining whether the requirements of Subsection
 12-19 (a) have been met, the burden of proof shall be on:

12-20 (1) the plaintiff limited partner if:

12-21 (A) the applicable person or persons making the
 12-22 determination under Section 153.404(a)(1) or (2) are independent
 12-23 and disinterested at the time the determination is made;

12-24 (B) the determination is made by a panel of one or
 12-25 more independent and disinterested individuals appointed under
 12-26 Section 153.404(a)(3); or

12-27 (C) the limited partnership presents prima facie
 12-28 evidence that demonstrates that the applicable person or persons
 12-29 making the determination under Section 153.404(a) are independent
 12-30 and disinterested; or

12-31 (2) the limited partnership in any other circumstance.

12-32 Sec. 153.409. ALLEGATIONS AFTER DEMAND REJECTED. If a
 12-33 derivative proceeding is instituted after a demand is rejected, the
 12-34 petition must allege with particularity facts that establish that
 12-35 the rejection was not made in accordance with the requirements and
 12-36 standards under Sections 153.404 and 153.408.

12-37 Sec. 153.410. DISCONTINUANCE OR SETTLEMENT. (a) A
 12-38 derivative proceeding may not be discontinued or settled without
 12-39 court approval.

12-40 (b) The court shall direct that notice be given to the
 12-41 affected partners if the court determines that a proposed
 12-42 discontinuance or settlement may substantially affect the
 12-43 interests of other partners.

12-44 Sec. 153.411. PAYMENT OF EXPENSES. (a) In this section,
 12-45 "expenses" means reasonable expenses incurred by a party in a
 12-46 derivative proceeding, including:

12-47 (1) attorney's fees;

12-48 (2) costs in pursuing an investigation of the matter
 12-49 that was the subject of the derivative proceeding; or

12-50 (3) expenses for which the limited partnership may be
 12-51 required to indemnify another person.

12-52 (b) On termination of a derivative proceeding, the court may
 12-53 order:

12-54 (1) the limited partnership to pay expenses the
 12-55 plaintiff incurred in the proceeding if the court finds the
 12-56 proceeding has resulted in a substantial benefit to the limited
 12-57 partnership;

12-58 (2) the plaintiff to pay expenses the limited
 12-59 partnership or other defendant incurred in investigating and
 12-60 defending the proceeding if the court finds the proceeding has been
 12-61 instituted or maintained without reasonable cause or for an
 12-62 improper purpose; or

12-63 (3) a party to pay expenses incurred by another party
 12-64 relating to the filing of a pleading, motion, or other paper if the
 12-65 court finds the pleading, motion, or other paper:

12-66 (A) was not well grounded in fact after
 12-67 reasonable inquiry;

12-68 (B) was not warranted by existing law or a good
 12-69 faith argument for the application, extension, modification, or

13-1 reversal of existing law; or
 13-2 (C) was interposed for an improper purpose, such
 13-3 as to harass, cause unnecessary delay, or cause a needless increase
 13-4 in the cost of litigation.

13-5 Sec. 153.412. APPLICATION TO FOREIGN LIMITED
 13-6 PARTNERSHIPS. (a) In a derivative proceeding brought in the right
 13-7 of a foreign limited partnership, the matters covered by this
 13-8 subchapter are governed by the laws of the jurisdiction of
 13-9 formation of the foreign limited partnership, except for Sections
 13-10 153.405, 153.410, and 153.411, which are procedural provisions and
 13-11 do not relate to the internal affairs of the foreign limited
 13-12 partnership, unless applying the laws of the jurisdiction of
 13-13 formation of the foreign limited partnership requires otherwise
 13-14 with respect to Section 153.405.

13-15 (b) In the case of matters relating to a foreign limited
 13-16 partnership under Section 153.405, a reference to a person or group
 13-17 of persons described by Section 153.404 refers to a person or group
 13-18 entitled under the laws of the jurisdiction of formation of the
 13-19 foreign limited partnership to make the determination described by
 13-20 Section 153.404(a). The standard of review of a determination made
 13-21 by the person or group shall be governed by the laws of the
 13-22 jurisdiction of formation of the foreign limited partnership.

13-23 Sec. 153.413. CLOSELY HELD LIMITED PARTNERSHIP. (a) In
 13-24 this section, "closely held limited partnership" means a limited
 13-25 partnership that has:

13-26 (1) fewer than 35 limited partners; and
 13-27 (2) no partnership interests listed on a national
 13-28 securities exchange or regularly quoted in an over-the-counter
 13-29 market by one or more members of a national securities association.

13-30 (b) Sections 153.402-153.410 do not apply to a claim or a
 13-31 derivative proceeding by a limited partner of a closely held
 13-32 limited partnership against a general partner, limited partner, or
 13-33 officer of the limited partnership. In the event the claim or
 13-34 derivative proceeding is also made against a person who is not that
 13-35 general partner, limited partner, or officer, this subsection shall
 13-36 apply only to the claim or derivative proceeding against the
 13-37 general partner, limited partner, or officer.

13-38 (c) If Sections 153.402-153.410 do not apply because of
 13-39 Subsection (b) and if justice requires:

13-40 (1) a derivative proceeding brought by a limited
 13-41 partner of a closely held limited partnership may be treated by a
 13-42 court as a direct action brought by the limited partner for the
 13-43 limited partner's own benefit; and

13-44 (2) a recovery in a direct or derivative proceeding by
 13-45 a limited partner may be paid directly to the plaintiff or to the
 13-46 limited partnership if necessary to protect the interests of
 13-47 creditors or other partners of the limited partnership.

13-48 (d) Other provisions of state law govern whether a limited
 13-49 partner has a direct cause of action or right to sue a general
 13-50 partner, limited partner, or officer, and this section may not be
 13-51 construed to create that direct cause of action or right to sue.

13-52 SECTION 31. The changes in law made by this Act apply only
 13-53 to a derivative proceeding instituted on or after the effective
 13-54 date of this Act. A derivative proceeding instituted before the
 13-55 effective date of this Act is governed by the law in effect on the
 13-56 date the proceeding was instituted, and the former law is continued
 13-57 in effect for that purpose.

13-58 SECTION 32. This Act takes effect September 1, 2019.

13-59

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