

## **Securities Regulation Daily Wrap Up, TOP STORY—Del. Sup. Ct.: Delaware corporations may restrict '33 Act claims to federal court, (Mar. 18, 2020)**

Securities Regulation Daily Wrap Up

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By [Anne Sherry, J.D.](#)

The Delaware Supreme Court reversed a chancery court decision invalidating federal-forum provisions that require Securities Act claims to be brought in federal court.

Reversing the Court of Chancery, the Delaware Supreme Court held that charter provisions requiring that Securities Act claims be brought in federal court are facially valid under Delaware law. While mindful of concerns that other states may not enforce the decision, the court rejected chancery's construction of a dichotomy between internal and external affairs. Instead, federal-forum provisions lie between these extremes on a continuum ([Salzberg v. Blue Apron Holdings, Inc.](#), March 18, 2020, Valihura, K.).

The three appellants in this case are Delaware corporations that adopted federal-forum provisions prior to their 2017 IPOs, providing that federal district courts are the exclusive forum for Securities Act claims. The U.S. Supreme Court in [Cyan](#) (U.S. 2018) held that state courts could preside over private lawsuits alleging only Securities Act claims. The response, according to a Cornerstone Research study, was a change in litigation strategy that had plaintiffs filing an increasing number of '33 Act cases in state court, sometimes resulting in parallel actions in both federal and state court.

The chancery court [invalidated](#) the federal-forum provisions based on "first principles," a conclusion that puzzled the academic and former SEC Commissioner Joseph Grundfest, whose relevant [paper](#) the Supreme Court cites in a footnote. According to the chancery court, a '33 Act claim relates to external rather than internal affairs of the company in that it "does not turn on the rights, powers, or preferences of the shares, language in the corporation's charter or bylaws, a provision in the DGCL, or the equitable relationships that flow from the internal structure of the corporation."

This analysis, the Delaware Supreme Court wrote, narrowed the broad scope of the provision of the Delaware General Corporation Law that governs what a corporation may include in its certificate of incorporation. Section 102(b)(1) authorizes: (1) any provision for the management of the business and conduct of the affairs of the corporation; and (2) any provision creating, defining, limiting, and regulating the powers of the corporation, the directors, and the stockholders, as long as it is not contrary to Delaware law. A federal-forum provision is facially valid because it could easily fall within either of these categories, the court said. There is no procedural mechanism to consolidate or coordinate parallel federal and state actions; by restricting Securities Act claims to federal courts, federal-forum provisions classically fit the first category of authorized provisions. Federal-forum provisions also fit the second category by prescribing where stockholders can bring Securities Act claims.

Federal-forum provisions are also not contrary to Delaware's policies or laws, the court explained. The Supreme Court took particular issue with the chancery court's reading of Section 102(b)(1) as limited to "internal affairs" matters under *Boilermakers* (Del. Ch. 2013). "By creating a binary world of only 'internal affairs' claims and 'external' claims, the Court of Chancery superimposed the 'internal affairs' doctrine onto and narrowed the scope of Section 102(b)(1)—contrary to its plain language." The Supreme Court included a Venn diagram in its opinion to illustrate that there are certain intra-corporate claims that are not within the high courts' scope of "internal affairs" but still fall within the DGCL, including Section 102(b)(1).

The Supreme Court acknowledged that the chancery court may have grounded its decision in "first principles" out of concern that other states may not be inclined to uphold federal-forum provisions. The high court

recognized that it is potentially problematic for Delaware to have a narrower definition of "internal affairs." And it devoted some space in its opinion to assuaging the "powerful concern" over whether other states will respect and enforce Delaware corporations' federal-forum provisions. While "Delaware historically has [been], and should continue to be, vigilant about not stepping on the toes of our sister states or the federal government," there are persuasive arguments that a federal-forum provision does not offend federal policy or principles of horizontal sovereignty, the court concluded.

The case is [No. 346, 2019](#).

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Companies: Blue Apron Holdings, Inc.; Stitch Fix, Inc.; Roku, Inc.

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