

## Delaware Supreme Court: Federal Forum Selection Provisions for Securities Act Claims Are Facially Valid

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On March 18, 2020, the Delaware Supreme Court held that forum selection provisions in certificates of incorporation requiring actions arising under the Securities Act of 1933 (the “Securities Act”) to be filed in federal court are facially valid under Section 102(b)(1) of the Delaware General Corporation Law (“DGCL”).<sup>[1]</sup> *Salzberg v. Sciabacucchi*, 2020 WL 1280785 (Del. 2020) (Valihura, J.). The court recognized that federal forum provisions (“FFPs”) “can provide a corporation with certain efficiencies in managing the procedural aspects of securities litigation following the United States Supreme Court’s decision in *Cyan, Inc. v. Beaver County Employees Retirement Fund*,” 138 S. Ct. 1061 (2018), which held that state courts have concurrent jurisdiction over actions asserting Securities Act claims.<sup>[2]</sup>

### Background

The Delaware Supreme Court reversed a Chancery Court decision holding that FFPs are “ineffective and invalid.” *Sciabacucchi v. Salzberg*, 2018 WL 6719718 (Del. Ch. Dec. 19, 2018).<sup>[3]</sup> The Chancery Court based its decision on *Boilermakers Local 154 Ret. Fund v. Chevron Corp.*, 73 A.3d 934 (Del. Ch. 2013), which held that companies may adopt forum selection bylaws requiring “internal affairs” litigation to be brought in Delaware Chancery Court.<sup>[4]</sup> The *Boilermakers* court indicated that it would have reached a different conclusion if the forum selection bylaws at issue “regulat[ed] external matters” by, for example, reaching tort claims or commercial contract claims. The *Sciabacucchi* court held that a forum-selection provision cannot govern Securities Act claims because such claims are “external to the corporation.” 2018 WL 6719718. The court reasoned that such a claim “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.”

### Section 102(b)(1) Is Not Limited to “Internal Affairs” Matters

The Delaware Supreme Court found that “*Boilermakers* did not establish the outer limit of what is permissible under . . . Section 102(b)(1).” The Court explained that “[t]here is a category of matters that is situated on a continuum between the *Boilermakers* definition of ‘internal affairs’ and its description of purely ‘external’ claims,” and held that this category falls within “the universe of matters encompassed by Section 102(b)(1).” The Court found that claims under Section 11 of the Securities Act “are ‘internal’ in the sense that they arise from internal corporate conduct on the part of the Board and, therefore, fall within Section 102(b)(1).”

The Court found that its earlier decision in *ATP Tour v. Deutscher Tennis Bund*, 91 A.3d 554 (Del. 2014), supports this conclusion. The ATP Court held that a litigation fee-shifting bylaw is facially valid.<sup>[5]</sup> The *Sciabacucchi* Court found that “ATP suggests that certificate of incorporation provisions governing certain types of ‘intracorporate’ claims that are not strictly within *Boilermakers*’ ‘internal affairs,’ can be within the boundaries of . . . Section 102(b)(1).”

The Delaware Supreme Court further held that Section 115 of the DGCL, which was enacted in 2015 to codify the *Boilermakers* holding, does not limit the scope of Section 102(b)(1).<sup>[6]</sup> Section 115 governs forum selection provisions concerning “internal corporate claims.” The Court found that “Section 102(b)(1) is unquestionably broader than, and is not circumscribed by, Section 115’s definition of ‘internal corporate claims.’”

### **FFPs Fall Within the Broad Scope of Section 102(b)(1)**

Section 102(b)(1) provides that a company’s certificate of incorporation may include:

Any provision for the management of the business and for the conduct of the affairs of the corporation, and any provision creating, defining, limiting and regulating the powers of the corporation, the directors, and the stockholders . . . if such provisions are not contrary to the laws of this State.

8 Del. C. § 102(b)(1). The Court found that an FFP “could easily fall within either of these broad categories.” The Court explained that “FFPs involve a type of securities claim related to the management of litigation arising out of the Board’s disclosures to current and prospective stockholders in connection with an IPO or secondary offering.” The Court further noted that “[t]he drafting, reviewing, and filing of registration statements by a corporation and its directors is an important aspect of a corporation’s management of its business and affairs and its relationship with its stockholders.” The Court also found that “FFPs do not violate the policies or laws of this State” as “the DGCL allows immense freedom for businesses to adopt the most appropriate terms for the organization, finance, and governance of their enterprise.”

The Court observed that since the United States Supreme Court’s decision in *Cyan*, there has been a sizable increase in Securities Act actions brought in state courts. The Court recognized that defending against parallel suits in federal and state courts involves “costs and inefficiencies,” as well as “[t]he possibility of inconsistent judgments and rulings on other matters, such as stays of discovery.” The Court explained that “[b]y directing [Securities Act] claims to federal courts when coordination and consolidation are possible, FFPs classically fit the definition of a provision ‘for the management of the business and for the conduct of the affairs of the corporation’” under Section 102(b)(1). The court further determined that “[a]n FFP would also be a provision ‘defining, limiting and regulating the powers of the corporation, the directors and the stockholders’ since FFPs prescribe where current and former stockholders can bring Section 11 claims against the corporation and its directors and officers.”

The Court concluded that “a bylaw that seeks to regulate the forum in which such ‘intra-corporate’ litigation can occur is . . . facially valid under Section 102(b)(1).”

### **FFPs Do Not Violate Federal Laws or Policies**

The Delaware Supreme Court determined that “FFPs do not violate federal law or policy.” The court explained that “nothing in *Cyan* prohibits a forum-selection provision from designating federal court as the venue for litigating Securities Act claims.” The court found it significant that in *Rodriguez de Quijas v. Shearson/American Express*, 490 U.S. 477 (1989), the United States Supreme Court enforced an arbitration provision that precluded the litigation of Securities Act claims in state court. The Delaware Supreme Court also noted that in *M/S Bremen v. Zapata Off-Shore Co.*, 407 U.S. 1 (1972), the United States Supreme Court directed “courts to give as much effect as possible to forum-selection clauses.” Because *Cyan* did not address or limit either *Bremen* or *Rodriguez*, the Delaware Supreme Court found that those rulings “still govern the enforcement of [forum selection] provisions.”

### **FFPs Do Not Violate Inter-State Policy**

The Delaware Supreme Court acknowledged that potentially “the most difficult aspect” of the question before it was “the ‘down the road’

question of whether [FFPs] will be respected and enforced by our sister states.” The Court recognized that other “states might react negatively” to its decision. Nevertheless, the Court concluded that there were “persuasive arguments” to be made that “a provision in a Delaware corporation’s certificate of incorporation requiring Section 11 claims to be brought in a federal court does not offend principles of horizontal sovereignty—just as it does not offend federal policy.” The Court reasoned that “many Section 11 claims closely parallel state law breach of fiduciary duty claims” and thus, “many of the same reasons requiring application of the internal affairs doctrine would support the enforcement of FFPs.” The Court stated that “[t]he need for uniformity and predictability that FFPs address suggest that they fall closer to the ‘internal affairs’ side of the spectrum, which would argue in favor of deference being given to them.” The Court emphasized that “forum-selection provisions are process-oriented,” and only “regulate *where* stockholders may file suit, not *whether* the stockholder may file suit or the kind of remedy that the stockholder may obtain on behalf of herself or the corporation.” Finally, the Court explained that other states have respected the types of “forum provisions sanctioned by *Boilermakers*,” which “are arguably more restrictive than FFPs . . . because they may require non-resident stockholders to litigate their internal affairs claims exclusively in Delaware—potentially far from their geographic home-base.” The court noted that “FFPs [merely] require that non-residents bring Section 11 claims in federal court (which could be in their home state).”

The Delaware Supreme Court emphasized that its ruling was limited to the facial challenge at issue. The Court explained that its sister courts could consider the enforcement of a particular FFP in an as-applied challenge and noted that “[s]uch ‘as applied’ challenges are an important safety valve in the enforcement context.”

[1] Section 102(b)(1) sets forth certain categories of provisions that may be included in a certificate of incorporation.

[2] Please [click here](#) to read our discussion of the Supreme Court’s decision in *Cyan*.

[3] Please [click here](#) to read our discussion of the Delaware Chancery Court’s decision in *Sciabacucchi*.

[4] Please [click here](#) to read our discussion of the Delaware Chancery Court’s decision in *Boilermakers*.

[5] Please [click here](#) to read our discussion of the Delaware Supreme Court’s decision in *ATP*.

[6] Section 115 provides that “[t]he certificate of incorporation or the bylaws may require, consistent with applicable jurisdictional requirements, that any or all internal corporate claims shall be brought solely and exclusively in any or all of the courts in this State, and no provision of the certificate of incorporation or the bylaws may prohibit bringing such claims in the courts of this State.” 8 *Del. C.* § 115. Section 115 defines “internal corporate claims” to include “claims . . . that are based upon a violation of a duty by a current or former director or officer or stockholder in such capacity.” *Id.*

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