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IN THE SUPREME COURT OF THE STATE OF DELAWARE

MATTHEW B. SALZBERG, JULIE M.B. BRADLEY, TRACY BRITT COOL, KENNETH A. FOX, ROBERT P. GOODMAN, GARY R. HIRSHBERG, BRIAN P. KELLEY, KATRINA LAKE, STEVEN ANDERSON, J. WILLIAM GURLEY, MARKA HANSEN, SHARON MCCOLLAM, ANTHONY WOOD, RAVI AHUJA, SHAWN CAROLAN, JEFFREY HASTINGS, ALAN HENDRICKS, NEIL HUNT, DANIEL LEFF, and RAY ROTHROCK, Defendants Below-Appellants, - and – BLUE APRON HOLDINGS, INC., STITCH FIX, INC. and ROKU, INC., Nominal Defendants Below-Appellants, v. MATTHEW SCIABACUCCHI, on behalf of himself and all others similarly situated, Plaintiff Below-Appellee.	**No. 346, 2019** Court Below: Court of Chancery of the State of Delaware, C.A. No. 2017-0931-JTL

BRIEF OF LAW PROFESSORS AS *AMICI CURIAE* IN SUPPORT OF PLAINTIFF-APPELLEE AND AFFIRMANCE

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TABLE OF CONTENTS

TABLE OF AUTHORITIES

Page(s)

CASES

STATUTES AND RULES

INTEREST OF *AMICI CURIAE*

Amici are professors who study and teach in the areas of corporate and federal securities law. They are regularly cited as authorities on questions of corporate law and governance. Although they differ amongst themselves about the utility of federal securities class actions, they are united in their belief that Delaware corporate law does not permit a corporate charter or bylaw provision to require claims arising under the federal securities laws to be resolved in any specified venue. The names and titles of the *Amici* are set forth in the Motion of Law Professors to File Brief as *Amici Curiae* in Support of Plaintiff-Appellee and Affirmance.

This appeal raises the question whether a Delaware corporation may, in its certificate of incorporation, require claims under the Securities Act of 1933 to be brought in federal court. *Amici's* brief addresses this question.

SUMMARY OF ARGUMENT

The United States Congress, when passing the Securities Act of 1933 (the "1933 Act") and the numerous subsequent federal statutes that touch upon and alter the rights and powers set forth in that Act, has repeatedly elected to give investors aggrieved by alleged violations of the 1933 Act the opportunity to pursue claims in either federal or state courts. In this action, the Court of Chancery correctly invalidated a charter provision requiring claims under the 1933 Act to be brought in federal court.

The leading authority on the propriety under Delaware law of a charter or bylaw provision requiring claims to be brought in a specified venue is the opinion of then-Chancellor Strine in *Boilermakers Local 154 Retirement Fund v. Chevron Corp.*[1] In *Chevron*, the court upheld as facially valid a bylaw provision that required internal affairs claims be brought in Delaware *because* the bylaws "only regulate[d] suits brought by stockholders as stockholders in cases governed by the internal affairs doctrine."[2] In so holding, the court contrasted a hypothetical bylaw that regulated "external matters"—such as a bylaw that purported to bind a stockholder plaintiff who sought to bring a tort claim based on a personal injury she suffered—which the court stated "would be beyond the statutory language of 8 *Del. C.* §109(b)"

[1] 73 A.3d 934 (Del. Ch. 2013)
[2] *Id.* at 939.

for the "obvious" reason that the bylaw "would not deal with the rights and powers of the plaintiff-stockholder *as a stockholder*."[3] Thus, under *Chevron*, the operative question in determining the validity of the charter provisions at issue in this litigation is whether they deal with the rights and powers of a stockholder as a stockholder, *i.e.*, whether the provisions regulate the internal affairs of the corporation.

Appellants and Appellants' *amici curiae* misread this Court's subsequent decision in *ATP Tour v. Deutscher Tennis Bund*,[4] which is fully consistent with *Chevron*. In *ATP*, this Court addressed, in relevant part, a certified question as to the facial validity of a Delaware corporation's bylaw shifting litigation expenses to unsuccessful plaintiffs in intra-corporation litigation. Critically, the underlying suit involved both antitrust claims *and* fiduciary duty claims. The Court held the bylaw facially valid—meaning it operated lawfully in at least one circumstance (*i.e.*, with respect to the fiduciary duty claims)—without reaching the question of whether the bylaw would have been valid had the litigation involved only antitrust claims. Nothing in *ATP* suggests that, if the Court was confronted with that question, it would have answered in the affirmative. Read together, *Chevron* and *ATP* teach that the "flexible contract" permitted by the Delaware General Corporation Law ("DGCL") and reflected in the charter and bylaws can cover much ground. They,

[3] *Id.* at 952.
[4] 91 A.3d 554 (Del. 2014)

however, cannot alter or limit rights given to individuals by sources of law external to Delaware's corporate law regime, based solely on the happenstance of those individuals also being stockholders.

A Delaware corporation's charter and bylaws cannot regulate where investors in registered offerings bring claims under the 1933 Act because such claims are external to the corporation. Congress chose to make Section 11 and Section 12 claims only available to the purchaser of a security in a registered offering and to link those claims to conduct giving rise to the purchase itself. Nothing in the 1933 Act requires the plaintiff to have been a pre-existing stockholder. Thus, while a 1933 Act claim may, by coincidence, share some similarities with a fiduciary duty claim, the plaintiff's status as a stockholder is irrelevant to the federal claim. Regardless of any similarities, the 1933 Act claim is external because it does not "deal with the rights and powers of the plaintiff-stockholder *as a stockholder*."[5]

Reversing the Court of Chancery's decision would constitute a substantial extension of the corporate contract and would infringe upon the will of Congress. Delaware law is entitled to and should not hesitate to regulate the internal affairs of its corporations, but should be careful not to overstep its "lane."

[5] *Chevron*, 73 A.3d at 952.

ARGUMENT

I. A DELAWARE CORPORATION'S CHARTER AND BYLAWS CAN ONLY REGULATE THE CORPORATION'S INTERNAL AFFAIRS

The linchpin of Delaware's assumption of stockholder consent to director-only alteration of bylaws and generally broad contractual enforcement of charters and bylaws alike is, necessarily, a properly tailored application of the internal affairs doctrine. Permitting those corporate contracts to affect, impair, or limit the ability of individuals who happen to be stockholders to exercise legal rights that exist completely independent of Delaware law is inconsistent with state corporate law and would constitute an ill-advised policy shift.

This Court should not extend the corporate contract beyond a Delaware corporation's internal affairs. Nor should it endorse the revision of the internal affairs doctrine Appellants seek. The leading authorities for interpreting the scope of Sections 102(b)(1) and 109(b) of the DGCL and of the corporate contract—which provide guidance as to the propriety of a charter or bylaw provision purporting to affect rights granted by the federal securities laws—are then-Chancellor Strine's opinion in *Boilermakers Local 154 Retirement Fund v. Chevron Corp.*,[6] and this Court's subsequent opinion in *ATP Tour v. Deutscher Tennis Bund*.[7]

[6] 73 A.3d 934 (Del. Ch. 2013).
[7] 91 A.3d 554 (Del. 2014).

Resting on the notion that the DGCL and a corporation's charter and bylaws constitute a "flexible contract" to which stockholders are a party,[8] those opinions uphold bylaw provisions requiring that claims arising under the DGCL and Delaware corporate law be litigated in a specified forum, and that attorney's fees and expenses in such litigation be borne by unsuccessful plaintiff stockholders.[9] Those opinions, however, also make clear that despite the breadth of permissible charter and bylaw provisions adopted pursuant to Sections 102(b)(1) and 109(b), the statute cannot be read to authorize provisions specifically dictating where litigation under the federal securities laws can be pursued because such litigation does not arise from the internal affairs of a corporation.

In *Chevron*, then-Chancellor Strine interpreted the plain text of Section 109(b)—which parallels Section 102(b)(1) in scope—to permit a bylaw that he considered to affect forum selection, but specifically because the bylaw only affected "the kind of claims most central to the relationship between those who manage the

[8] *Chevron*, 73 A.3d at 940 ("[O]ur Supreme Court has long noted that bylaws, together with the certificate of incorporation and the broader DGCL, form part of a flexible contract between corporations and stockholders, in the sense that the certificate of incorporation may authorize the board to amend the bylaws' terms and that stockholders who invest in such corporations assent to be bound by board-adopted bylaws when they buy stock in those corporations.").

[9] The latter proposition, set forth in *ATP*, was legislatively overruled in 2015. 80 Del. Laws, c. 40, §§ 2-3.

corporation and the corporation's stockholders" – namely, "suits brought by stockholders *as stockholders in cases governed by the internal affairs doctrine*."[10]

The court went out of its way to distinguish a bylaw regulating "external" matters, such as "a bylaw that purported to bind a plaintiff, even a stockholder plaintiff, who sought to bring a tort claim against the company based on a personal injury she suffered that occurred on the company's premises or a contract claim based on a commercial contract with the corporation."[11] A bylaw regulating selection of a forum to litigate external claims, the court held, "would be beyond the statutory language of 8 *Del. C.* 109(b)" for the "obvious" reason that it "would not deal with the rights and powers of the plaintiff-stockholder *as a stockholder*."[12] Thus, the court expressly stated, a forum selection bylaw could *not* regulate a securities fraud claim because such claims are external to the corporation.[13] In sum, *Chevron* teaches that the validity of a bylaw regulating forum selection turns on whether the claims pursued involve the internal affairs of the corporation.

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[10] *Id.* at 939, 952 (emphasis added).
[11] *Id.* at 952.
[12] *Id.*
[13] *See id.* at 962 ("Thus, FedEx's bylaw is consistent with what has been written about similar forum selection clauses addressing internal affairs cases: '[Forum selection] provisions do not purport to regulate *a stockholder's ability to bring a securities fraud claim* or any other claim that *is not an intra-corporate matter*.'") (quoting Joseph A. Grundfest & Kristen A. Savelle, *The Brouhaha over Intra–Corporate Forum Selection Provisions: A Legal, Economic, and Political Analysis,* 68 Bus. Law. 325, 370 (2013) (emphasis added)).

Nothing in *ATP* alters this sensible outcome. Addressing the principal certified question in that case, the Court was necessarily focused on "suits brought by stockholders as stockholders in cases *governed by the internal affairs doctrine*."[14] In the underlying litigation, the plaintiffs alleged "Delaware fiduciary duty claims," as well as antitrust claims. Nothing in the *ATP* opinion questioned former Chancellor Strine's view that the "flexible contract" formed by the statute, charter, and bylaws could *not* extend to any litigation other than cases governed by the internal affairs doctrine.

Indeed, if the underlying suit involved only antitrust claims, we expect that the Court would have ruled (consistent with *Chevron*) that the bylaw could not have provided for fee-shifting based solely on the antitrust plaintiff's happenstance of also being a stockholder. Importantly, having been asked merely to assess the facial validity of the bylaw, the Court had no occasion to determine whether the bylaw could impose shifting fees solely attributable to the antitrust claims.

In sum, as *Chevron* expressly teaches, while the "flexible contract" permitted by the DGCL and reflected in a company's certificate of incorporation and bylaws can cover much ground, it is not limitless. In our view, as a matter of Delaware corporate law, the "flexible contract" cannot extend so far as to permit the charter or bylaws to regulate disputes external to the corporation.

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[14] *Id.* at 939.

II. 1933 ACT CLAIMS ARE EXTERNAL TO THE CORPORATION

Direct suits to enforce rights created by the United States Congress through the federal securities laws necessarily represent claims external to the corporation. Sections 11 and 12, like Rule 10b-5, arise from the purchase or sale of a security; they do not arise out of the plaintiff's status as a stockholder.

Even when Congress and Delaware create rights that are coextensive and overlapping, Delaware law should be assiduous in limiting the scope of its regime to avoid needless conflict. To be sure, Congress showed its respect and appreciation for Delaware's important (but not unlimited) role in the regulation of corporate behavior by including the so-called "Delaware Carve-Out" to the Securities Litigation Uniform Standards Act of 1998. If Delaware now decides to permit its corporations to impose charter or bylaw provisions limiting the scope of rights that Congress specifically decided to provide a class of individuals who may or may not be stockholders of Delaware corporations, Congress may in the future be less deferential to Delaware's authority over internal affairs.

It is thus important to distinguish between claims created by another (*i.e.*, non-Delaware) body of law that may ultimately have some effect on a corporation, and claims arising from Delaware law that relate to traditional internal matters, such as derivative litigation based on an alleged breach of the directors' or officers' fiduciary duties. By definition, federal securities claims are not a right derived from the

"corporate contract." They exist and are derived from a statute created by a different sovereign. Therefore, as with other claims that are external to that contract, dictating the forum for pursuing federal securities claims is not a proper subject for charter or bylaw provisions.

As discussed above, in *Chevron*, the court distinguished between bylaws that govern "internal affairs," which the court found permissible based on a straightforward interpretation of Section 109(b), and claims external to the corporation, which the court held "would be beyond the statutory language of 8 *Del. C.* 109(b)" for the "obvious" reason that it "would not deal with the rights and powers of the plaintiff-stockholder *as a stockholder*."[15] For instance, the court observed that a provision purporting to govern a stockholder's ability to bring tort claims—*e.g.*, an attempt to create a forum selection clause that would apply to a products liability claim brought by a purchaser of a defective product who also happened to be a stockholder of the defendant company—would be improper.

By the same token, a bylaw purporting to regulate the litigation of claims under Rule 10b-5 "would not deal with the rights and powers of the plaintiff[] *as a stockholder*," and would therefore not fall within the broad scope of Sections 102(b)(1) or 109(b). The substance of a Rule 10b-5 claim relates to a fraud made "in connection with the purchase or sale of a security," and only a purchaser or seller

[15] *Id.* at 952.

may bring a claim.[16] Whether that individual is a stockholder of the Rule 10b-5 defendant is legally irrelevant. As the Delaware Court of Chancery has observed, "[a] Rule 10b-5 claim under the federal securities laws is a personal claim akin to a tort claim for fraud. The right to bring a Rule 10b-5 claim is not a property right associated with shares, nor can it be invoked by those who simply hold shares of stock."[17] In other words, a Rule 10b-5 claim is an external claim.

That rationale applies with equal force to Section 11 and Section 12 claims. Claims pursuant to Sections 11 and 12 are, by their statutory language, only available to the *purchaser* of a security in a registered offering and relate to conduct that gave rise to the purchase (*e.g.*, a misstatement in a registration statement or prospectus, or the sale of an unregistered security). The legally proscribed conduct takes place before or concurrent with the moment of the purchase, meaning that the claim actually arises out of an event that happened before the plaintiff became a stockholder subject to the corporate contract. A securities purchaser who is no longer a stockholder would still be eligible to bring a securities claim, yet not eligible to bring a derivative claim relating to the "internal" affairs of the corporation for lack

[16] *In re Activision Blizzard Inc. S'holder Litig.*, 124 A.3d 1025, 1056 (Del. Ch. 2015).
[17] *Id.* A logical extension of Appellants and Appellants' *amici curiae*'s position is that a corporation could adopt a charter provision regulating the forum for Rule 10b-5 litigation, such as by requiring all Rule 10b-5 claims be brought in Delaware federal court. It is axiomatic that such a charter provision would represent a substantial extension of the reach of state law.

of "continuous" relationship with the corporation. The mere possibility that a purchaser of shares in an IPO or other registered offering could have also held shares prior to the offering giving rise to the federally created claim is happenstance.

As the Court of Chancery correctly noted, although a Section 11 claim may be related to business matters in general, that is not sufficient to make it an internal affairs claim.[18] Many events plainly regulated by non-Delaware law regimes (and which fall beyond the scope of permissible charter or bylaw provisions) relate in some way to business matters. Take, for example, the Court of Chancery's apt hypothetical regarding the theft of a stock certificate: "[t]he fact that the stolen property consists of shares is incidental to the claim."[19] The theft claim does not arise out of the "flexible contract" between the corporation and its stockholders and is, therefore, external.

Likewise, if an employee of a corporation or other individual asserted a claim pursuant to the Employee Retirement Income Security Act, the Sherman Act, the Lanham Act, or the False Claims Act (as but a few examples), that individual's concurrent ownership of shares would be wholly incidental to the claim, rendering

[18] *See Sciabacucchi v. Salzberg*, 2018 WL 6719718, at *22 (Del. Ch. Dec. 19, 2018) ("Many aspects of the corporation's business and affairs involve external relationships. The certificate of incorporation and Delaware law cannot regulate those external relationships.").
[19] *Id.* at *2.

the claim external. As *Chevron* makes clear, such claims are not subject to alteration or limitation under Delaware law by a charter or bylaw provision.[20]

There are other aspects of traditional securities claims that demonstrate their external nature and the legislature's studious avoidance of internal affairs. For example, in interpreting the requirement that a claim under Rule 10b-5 be "in connection with the purchase or sale of a security," courts have repeatedly noted that "Congress by section 10(b) did not seek to regulate transactions which constitute no more than internal corporate mismanagement."[21]

Moreover, as "security" has a broader meaning than "stock,"[22] and corporations may offer securities other than stock, such claims might be governed

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[20] Although we see it as axiomatic that such claims fall beyond the permissible reach of charter and bylaw provisions, that may no longer be the case if the Court embraces Appellants' position. If a charter provision can regulate 1933 Act claims, why could it not also regulate tort claims that relate to the corporation, but do not arise out of the stockholder's status as a stockholder?

[21] *Superintendent of Insurance v. Bankers Life & Casualty Co.*, 404 U.S. 6, 12 (1971). *See also, e.g.*, *Santa Fe Indus. Inc. v. Green*, 430 U.S. 462, 479 (1977) (same).

[22] *See* 15 U.S.C. § 77b(a)(1) ("The term 'security' means any note, stock, treasury stock, security future, security-based swap, bond, debenture, evidence of indebtedness, certificate of interest or participation in any profit-sharing agreement, collateral-trust certificate, preorganization certificate or subscription, transferable share, investment contract, voting-trust certificate, certificate of deposit for a security, fractional undivided interest in oil, gas, or other mineral rights, any put, call, straddle, option, or privilege on any security, certificate of deposit, or group or index of securities (including any interest therein or based on the value thereof), or any put, call, straddle, option, or privilege entered into on a national securities exchange relating to foreign currency, or, in general, any interest or instrument commonly known as a "security", or any certificate of interest or participation in,

by securities law but not subject to a conventional state corporate law fiduciary duty claim.[23] Finally, the statutorily enumerated defendants for typical Section 11 claims are simply not "internal" to the corporation, as the list of enumerated defendants in Section 11 of the 1933 Act purposely and specifically permits plaintiffs to sue those who are not officers or directors of the corporation, including underwriters and accountants.

In summary, Delaware law does not and should not permit the charter or bylaws to dictate the forum for federal securities actions, because the right to bring such actions is not a property right associated with shares of corporate stock. The forum for federal securities actions thus falls outside of the scope of what Delaware law permits the corporate charter and bylaws to regulate.

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temporary or interim certificate for, receipt for, guarantee of, or warrant or right to subscribe to or purchase, any of the foregoing.")

[23] *See*, *e.g.*, *North Am. Catholic Educ. Programming Found., Inc. v. Gheewalla*, 930 A.2d 92, 101 (Del. 2007).

CONCLUSION

For the reasons set forth herein, *Amici* respectfully urge this Court to affirm the judgement of the Court of Chancery.

November 1, 2019

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