Client Alert: A Significant Legal Victory for Delaware Companies Filing Initial Public Offerings and Secondary Offerings

The *Sciabacucchi* decision represents a victory for Delaware incorporated companies.

Companies incorporated in Delaware can now avail themselves of the "flexibility and wide discretion" that the Delaware General Corporation Law ("DGCL") allows by proscribing, in their corporate charters, a requirement that shareholder suits under the Securities Act of 1933 ('Securities Act") must be commenced in a federal forum. The ruling has profound implications on a Delaware corporation's ability to direct where its shareholders can bring litigation arising out of the company's public registration filings.

On March 18, 2020, in a unanimous decision, the Delaware Supreme Court ("Court") held that corporate charter provisions requiring claims under the Securities Act to be litigated in federal court, are facially valid.[1] The Court reviewed the underlying December 2018 decision from the Delaware Chancery Court that held federal forum selection provisions were invalid and unenforceable. Forum selection provisions were a proposed solution to the U.S. Supreme Court's *Cyan*[2] decision in March 2018, in which the U.S. Supreme Court held plaintiff shareholders could file Securities Act claims in both federal and state court; allowing state court concurrent jurisdiction under the Securities Act.

In *Sciabacucchi*, the Court reversed the Chancery Court, reasoning that federal forum provisions were a valid form of "private ordering." The court scrutinized what the DGCL meant by "internal affairs" and found that the federal forum provisions did not contradict Delaware law, nor the legislative intent of the DGCL. The court also noted that nothing in *Cyan* prohibits a forum selection provision from designating federal court as the venue for litigating Securities Act claims.

In holding that federal forum provisions are facially valid, the Delaware Supreme Court acknowledged that federal forum provisions, targeting Securities Act claims, "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 continued that registration statements are "an important aspect of a corporation's management of its business affairs and of its relationship with its stockholders." Further, the court reasoned that a "bylaw that seeks to regulate the forum in which such 'intra-corporate' litigation can occur is a provision that addresses the 'management of the business' and the 'conduct of the affairs of the corporation,' and is thus, facially valid under Section 102(b)(1)."

The Court's opinion struck an academic cord in its analysis of the distinction between the "internal and external affairs" of a Delaware corporation. The Court noted that the Chancery Court's finding was flawed when it concluded that "everything other than an 'internal affairs' claim was 'external' and therefore not the proper subject of a bylaw or charter provision." Further, the Court found federal forum provisions dictating the forum for Section 11 claims "are neither 'external' nor 'internal affairs' claims. Rather, they are in-between in what might be called Section 102(b)(1)'s 'Outer Band' and falling 'Outer Band'", meaning federal forum provisions are facially valid. The Court even utilized a 'Venn diagram' graphic to illustrate its reasoning. (See, Opinion)

Conclusion

The Court concluded its opinion citing several public policy-based reasons to further support the finding. It stated federal forum provisions do not "offend federal law and policy, nor do they offend principles of horizontal sovereignty." Moreover, the federal forum provisions align with the Court's goals of "judicial economy" and avoidance of "duplicative effort." Finally, in recognizing Delaware corporations' ability to adopt innovative corporate governance provisions, the Court concluded by averring, "that a board's action might involve a new use of plain statutory authority does not make it invalid under our law, and the board of Delaware corporations have the flexibility to respond to changing dynamics in ways that are authorized by our statutory law." The *Sciabacucchi* decision represents a victory for Delaware incorporated companies by permitting them to craft a federal forum provision in their charters and muting the repercussions of *Cyan*.

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[1] *Sciabacucchi v. Salzberg, Del. Supr.*, No. 346, 2019, Valihura, K. (March 18, 2020) (ORDER).

[2] *Cyan, Inc. v. Beaver Cty. Emples. Ret. Fund,* 138 S. Ct. 1061 (2018)

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