St. John's Law Review

Volume 94
Number 3 *Volume 94, Fall 2021, Number 3*

Article 7

Arbitrating Security Class Actions: The Limits of Forum Selection Bylaws

Paul Schochet

ARBITRATING SECURITY CLASS ACTIONS: THE LIMITS OF FORUM SELECTION BYLAWS

PAUL SCHOCHET[†]

INTRODUCTION

In November 2018, The Doris Behr 2012 Irrevocable Trust offered a shareholder proposal[1] "to adopt a mandatory arbitration bylaw" in Johnson & Johnson's annual proxy[2] statement.[3] Led by

---

[†] Notes & Comments Editor, *St. John's Law Review* and *Journal of Catholic Legal Studies*; J.D. Candidate 2021, St. John's University School of Law; B.A., 2016, University of Delaware. I thank my Note advisor, Dean Michael A. Perino, for his invaluable insight and guidance. I am also grateful to my father, Ira A. Schochet, for inspiring this Note topic and for his thoughtful comments.

[1] The proposal states, in part:

> The shareholders of [Johnson & Johnson] request the Board of Directors take all practicable steps to adopt a mandatory arbitration bylaw that provides:
>
> > for disputes between a stockholder and the Corporation and/or its directors, officers or controlling persons relating to claims under federal securities laws in connection with the purchase or sale of any securities issued by the Corporation to be exclusively and finally settled by arbitration under the Commercial Rules of the American Arbitration Association (AAA), as supplemented by the Securities Arbitration Supplementary Procedures.

Doris Behr 2012 Irrevocable Tr. v. Johnson & Johnson, No. 19-8828, 2019 WL 1519026, at *1 & n.1 (D.N.J. Apr. 8, 2019) (quoting the Doris Behr 2012 Irrevocable Trust's proxy proposal).

[2] Memorandum of Law in Support of Defendant Johnson & Johnson's Motion to Dismiss at 7, *Doris Behr 2012 Irrevocable Tr.*, 2019 WL 1519026 (No. 19-8828) [hereinafter Brief for Defendant]. A Proxy statement is a required Securities and Exchange Commission ("SEC") document provided by the corporation to its shareholders that contains information concerning "voting procedure, nominated candidates for its board of directors, and compensation of directors and executives." Alicia Tuovila, *Proxy Statement*, INVESTOPEDIA, https://www.investopedia.com/terms/p/proxystatement.asp [https://perma.cc/YH7V-FPR9] (last updated Oct. 30, 2020). This document is meant to ensure shareholders are up to date with all germane information heading into an annual or special stockholder meeting. *Id.*

[3] 17 C.F.R. § 240.14a-1(g) (2020). A corporation must include a shareholder proposal in its proxy statement unless the corporation can identify a procedural or substantive exception. *See* Trinity Wall St. v. Wal-Mart Stores, Inc., 792 F.3d 323, 335–36 (3d Cir. 2015) (discussing 17 C.F.R. § 240.14a-8).

Professor Hal Scott,[4] the shareholder's proposal would ban class action shareholder disputes and require investors to resolve federal securities disputes through arbitration.[5]

Predictably, the Doris Behr 2012 Irrevocable Trust proxy proposal set off a flurry of legal actions. Johnson & Johnson first proposed to exclude the proposal from its proxy materials, and sought no-action letter to that end from the Securities and Exchange Commission ("SEC"), claiming that, if implemented, the arbitration bylaw would require the Company to violate state law.[6] In February 2019, the staff of the SEC agreed with Johnson & Johnson and issued the requested no-action letter[7] based on New Jersey state law. The staff's decision, however, did not end the matter. The same shareholder filed an action in federal court in New Jersey[8] seeking to enjoin Johnson & Johnson's April 25 annual meeting because, according to the complaint, the Company improperly excluded its proposal.[9] The New Jersey District Court denied Plaintiff's motion for a preliminary injunction.[10] Later, in June 2021, the district court granted Johnson & Johnson's motion to dismiss on mootness and ripeness grounds.[11]

---

[4] *See* Memorandum in Support of Motion to Dismiss of Proposed Intervenors California Public Employees' Retirement System and Colorado Public Employees' Retirement Ass'n at 5, *Doris Behr 2012 Irrevocable Tr.*, 2019 WL 1519026 (No. 19-8828).

[5] *See* Complaint at 4, *Doris Behr 2012 Irrevocable Tr.*, 2019 WL 1519026 (No. 19-8828).

[6] Brief for Defendant, *supra* note 2, at 8. Johnson & Johnson benefited from an unsolicited letter from the New Jersey Attorney General stating that the arbitration bylaw would violate state law. *Id.* at 1–2.

[7] Skadden, Arps, Slate, Meagher & Flom, LLP, SEC No-Action Letter, 2018 WL 6584469 (Feb. 11, 2019). Subsequently, Johnson & Johnson filed its proxy material without the Doris Behr 2012 Irrevocable Trust's proposal under SEC Rule 14a-8(i)(2), which permits the exclusion of proposals that would violate either state or federal law. *See* Brief for Defendant, *supra* note 2, at 2.

[8] *See* Complaint, *Doris Behr 2012 Irrevocable Tr.*, 2019 WL 1519026 (No. 19-8828).

[9] *See* Alison Frankel, *Shareholder Pushing for Mandatory Arbitration Seeks To Block J&J's Annual Meeting*, REUTERS (Mar. 27, 2019, 4:23 PM), https://www.reuters.com/article/us-otc-j-j/shareholder-pushing-for-mandatory-arbitration-seeks-to-block-jjs-annual-meeting-idUSKCN1R82DD [https://perma.cc/J6UT-TT3X].

[10] *Doris Behr 2012 Irrevocable Tr.*, 2019 WL 1519026, at *5.

[11] Doris Behr 2012 Irrevocable Tr. v. Johnson & Johnson, No. 19-8828, 2019 WL 2722569, at *3 (D.N.J. June 30, 2021) (finding that The Doris Behr 2012 Irrevocable Trust's claim is moot because "it seeks a declaration regarding past conduct"); *id.* at *4 ("[T]he Court agrees that Plaintiffs' request is not ripe because any controversy with respect to a proposal that the Trust might submit in connection with future shareholder meetings is hypothetical at this juncture and contingent on future events. . . .").

While the Doris Behr Irrevocable Trust's arbitration proposal is uncommon, it is not new. For instance, in 2012, shareholders of Gannett and Pfizer sought to include an arbitration bylaw in each company's respective proxy materials, but the SEC permitted both companies to exclude the proposal[12] because, according to the SEC, it would violate federal law.[13] Unlike the Johnson & Johnson proposal, which narrowly covered "claims under federal securities laws,"[14] the proposal from both the Gannett and Pfizer shareholders used more capacious language to cover "[a]ny controversy or claim brought directly or derivatively."[15] More recently, the trustee of CommonWealth REIT adopted a comparably broad arbitration bylaw, which covered all shareholder disputes.[16]

The dispute over the Johnson & Johnson arbitration provision is part of a larger debate over the enforceability of arbitration bylaws. Starting with *CommonWealth REIT*, litigation about attempts to add arbitration bylaws has begun to permeate state and federal courts. In these prior cases, courts found the arbitration bylaws adopted by the subject corporations enforceable by relying on recent pro-arbitration United States Supreme Court decisions.[17] Yet these courts devoted little to no analysis to whether state law permitted adopting such bylaws.[18] Outside the courtroom, scholars have also debated for years whether corporations may add mandatory arbitration clauses to bylaws for securities transactions.[19] As with the judicial opinions, the bulk of the

---

[12] *See* Hogan Lovells US LLP, SEC No-Action Letter, 2011 WL 6859124 (Feb. 22, 2012); Pfizer Inc., SEC No-Action Letter, 2012 WL 587597 (Feb. 22, 2012).

[13] Opponents of arbitration bylaws have argued that such proposals are unenforceable under both the Securities Act and the Securities Exchange Act antiwaiver provisions. *See* 15 U.S.C. §§ 77n, 78cc(a) (2018); *see also* Letter from James Cox, Brainerd Currie Professor of Law, Duke Univ. Sch. of L., to Mary Jo White, Chair, U.S. Sec. & Exch. Comm'n (Oct. 30, 2013) (on file with Duke University). While these Securities Acts-based claims are relevant to this Note's subject matter, they are not discussed.

[14] *See supra* text accompanying note 1.

[15] Hogan Lovells US LLP, SEC No-Action Letter, *supra* note 12.

[16] *See* Corvex Mgmt. LP v. CommonWealth REIT, No. 24-C-13-001111, 2013 WL 1915769 (Md. Cir. Ct. May 8, 2013).

[17] *See, e.g.*, *id.*; Katz v. CommonWealth REIT, No. 24-C-13-001299, slip op. at 21–22, 39–41 (Cir. Ct. Balt. Feb. 19, 2014); *see also* Delaware Cnty. Emps. Ret. Fund v. Portnoy, No. 13-10405, 2014 WL 1271528, at *16 (D. Mass. Mar. 26, 2014) (denying plaintiff's motion for declaratory judgment and permanent injunction on defendant's arbitration bylaw).

[18] *See* cases cited *supra* note 17.

[19] *See generally* Claudia H. Allen, *Bylaws Mandating Arbitration of Stockholder Disputes?*, 39 DEL. J. CORP. L. 751 (2015); Barbara Black, *Eliminating Securities Fraud Class Actions Under the Radar*, 2009 COLUM. BUS. L. REV. 802; Bradley J.

analysis, and thus disagreement, amongst these scholars concerned the application of the Federal Arbitration Act to corporate governance documents.[20]

This Note argues that bylaws providing for mandatory arbitration of federal securities law disputes are unenforceable under state corporate law. First, to be enforceable, bylaws must, traditionally, involve the corporation's internal affairs,[21] a choice of law principle, which in this case limits the control that the corporation can exercise over one of its key constituents—the shareholders. And treating issues concerning federal securities laws as "internal affairs" is a dubious proposition. Such laws are only concerned with individual transactions involving purchases or sales of the corporation's securities rather than the internal workings of the transacting corporation. Second, long-standing court precedent has either explicitly held that securities transactions do not affect a corporation's internal affairs, or that claims only tangentially related to the internal workings of a corporation are not governed by the internal affairs doctrine. Thus, such precedent militates towards the unenforceability of arbitration bylaws seeking to regulate federal securities transactions.[22]

Part I discusses why the mechanics of corporate class actions matter a great deal to corporations, shareholders, and academics. Part I also details both public and private strategies that opponents of securities class actions have taken to stymie such litigation. Part II examines the competing arguments about whether

---

Bondi, *Facilitating Economic Recovery and Sustainable Growth Through Reform of the Securities Class-Action System: Exploring Arbitration as an Alternative to Litigation*, 33 HARV. J.L. & PUB. POL'Y 607 (2010); Zachary D. Clopton & Verity Winship, *A Cooperative Federalism Approach to Shareholder Arbitration*, 128 YALE L.J.F. 169 (2018); Ann M. Lipton, *Manufactured Consent: The Problem of Arbitration Clauses in Corporate Charters and Bylaws*, 104 GEO. L.J. 583 (2016); Hal S. Scott & Leslie N. Silverman, *Stockholder Adoption of Mandatory Individual Arbitration for Stockholder Disputes*, 36 HARV. J.L. & PUB. POL'Y 1187 (2013); Paul Weitzel, *The End of Shareholder Litigation? Allowing Shareholders To Customize Enforcement Through Arbitration Provisions in Charters and Bylaws*, 2013 BYU L. REV. 65.

[20] *See generally, e.g.*, Allen, *supra* note 19; Lipton, *supra* note 19.

[21] *Cf.* Boilermakers Loc. 154 Ret. Fund v. Chevron Corp., 73 A.3d 934, 952 (Del. Ch. 2013) (explaining how bylaws are impermissible under Delaware law if they regulate matters external to the function of a business, in contrast to bylaws covering only internal affairs). As explained *infra* notes 126–152 and accompanying text, the Delaware Supreme Court has recently broken from this consensus. At the time of this Note, however, this decision stands as a glaring outlier.

[22] While a court would need to address the preemptive effect of the Federal Arbitration Act, this Note only examines the reach of the internal affairs doctrine. For a detailed discussion of the Federal Arbitration Act's applicability to corporate bylaws, see Lipton, *supra* note 19.

federal securities transactions are part of the internal affairs of a corporation.[23]

While there has been a shift among corporations to address litigation threats through private ordering, and the Delaware Chancery has mainly ratified these different private actions as consistent with the internal affairs doctrine, courts must eventually draw a line. Otherwise, courts risk the neutering of established doctrine that the incorporating state's law governs matters concerning a corporation's internal affairs. To that end, whether a claim implicates a corporation's internal affairs, special attention must be paid to what relation the parties have to the corporation, what act gives rise to the cause of action, and what source of law the claim turns on.

I. BACKGROUND

A. Types of Claims and Size of Dispute

Federal securities class action claims come in several iterations. But some of the most common ones involve either fraud in a public securities offering under the Securities Act of 1933[24] or violations of Rule 10b-5[25] promulgated under the Securities Exchange Act of 1934[26] for cases of fraud after the issuance of stock.[27] These causes of action allow shareholders to act as a "private attorney general"—enforcing federal law without relying on the SEC or Department of Justice to take action first.[28]

---

[23] Although the Johnson & Johnson litigation illustrates that corporate law can be challenged in all fifty states, this Note will focus primarily on Delaware law because of the special place that state holds in the United States for corporate governance. *See* Mullen v. Acad. Life Ins. Co., 705 F.2d 971, 973 n.3 (8th Cir. 1983) (discussing Delaware law "because of Delaware's position as a leader in the field of corporate law" and noting that the "courts of other states commonly look to Delaware law"). These court decisions, and others like it, are unsurprising as sixty percent of publicly traded companies are incorporated in Delaware. *See* Robert Anderson IV & Jeffrey Manns, *The Delaware Delusion*, CLS BLUE SKY BLOG (Aug. 3, 2015), https://clsbluesky.law.columbia.edu/2015/08/03/the-delaware-delusion/ [https://perma.cc/LY4U-9TH4].

[24] 15 U.S.C. § 77a (2018).

[25] 17 C.F.R. § 240.10b-5 (2018).

[26] 15 U.S.C. § 78a.

[27] Tom Baker & Sean J. Griffith, *Predicting Corporate Governance Risk: Evidence from the Directors' & Officers' Liability Insurance Market*, 74 U. CHI. L. REV. 487, 497–98 (2007); Weitzel, *supra* note 19, at 72.

[28] John C. Coffee, Jr., *Rescuing the Private Attorney General: Why the Model of the Lawyer as Bounty Hunter Is Not Working*, 42 MD. L. REV. 215, 218 (1983); *see also* Michael A. Perino, *Did the Private Securities Litigation Reform Act Work?*, 2003 U. ILL. L. REV. 913, 918 & n.17 (citing Associated Indus. of N.Y. State, Inc. v. Ickes, 134 F.2d 694, 704 (2d Cir.), *vacated*, 320 U.S. 707 (1943)).

Federal securities claims make up a significant proportion of class actions in federal court. To take one study as an example, between 2004 and 2005 shareholder securities suits made up forty-eight percent of all class actions pending in federal court.[29]

In addition, these suits involve a significant amount of potential monetary recovery. For instance, from 2005 to 2010 there were around 100 securities class actions in each of those years in federal court that ended in a settlement.[30] Of these roughly 100 suits a year, their aggregate settlements ranged from $7 billion to $17 billion per year.[31]

Further, while certain parties have called for the elimination of the practice area writ large,[32] these suits have remained prevalent throughout the industry. As of 2018, the securities industry "saw more companies on [United States] exchanges facing a greater threat of securities litigation than in any previous year."[33] Even more notable—and surprising considering actions by legislatures and courts to limit securities class action suits[34]—is that the 403 newly filed securities class action suits in 2018 "nearly double[d] the 1997–2017 [filing] average."[35]

B. Opponents

Although securities class action suits have many defenders,[36] such suits do not lack critics. For one, these opponents assert that such suits are an ineffective way to deter future malfeasance or to

---

[29] Weitzel, *supra* note 19, at 78.

[30] Brian T. Fitzpatrick, *An Empirical Study of Class Action Settlements and Their Fee Awards*, 7 J. EMPIRICAL LEGAL STUD. 811, 814 (2010).

[31] *Id.*

[32] *See, e.g.*, Hal Scott, *The SEC'S Misguided Attack on Shareholder Arbitration*, WALL ST. J.: OPINION (Feb. 21, 2019, 7:17 PM), https://www.wsj.com/articles/the-secs-misguided-attack-on-shareholder-arbitration-11550794645 [https://perma.cc/KFM2-KZQG].

[33] Alexander Aganin & John Gould, *Securities Class Action Filings—2018 Year in Review*, HARV. L. SCH. F. ON CORP. GOVERNANCE (Feb. 8, 2019), https://corpgov.law.harvard.edu/2019/02/08/securities-class-action-filings-2018-year-in-review/ [https://perma.cc/87ZG-DQDR].

[34] *See* Weitzel, *supra* note 19, at 80 (discussing the "heighten[ed] pleading requirements, expand[ed] safe harbors, limit[ations] [on] who can sue, cap[ped] damage amounts, [and] delay[ed] discovery" measures that legislatures have instituted to cut back on class action securities litigation).

[35] Aganin & Gould, *supra* note 33.

[36] *See, e.g.*, Daniel J. Morrissey, *Shareholder Litigation After the Meltdown*, 114 W. VA. L. REV. 531, 532–33 (2012); Jill E. Fisch, *Confronting the Circularity Problem in Private Securities Litigation*, 2009 WIS. L. REV. 333, 336; James D. Cox, *Making Securities Fraud Class Actions Virtuous*, 39 ARIZ. L. REV. 497, 499 (1997).

compensate shareholders harmed by fraud because the remedy for securities class action suits is, they claim, "pocket-shifting wealth transfers" among shareholders.[37] Put differently, when a shareholder class action suit settles, the money the shareholders receive comes from the company, which ultimately comes from the shareholders.[38] Another critique lodged at shareholder class action suits involves the costs, both in the billions paid to defense attorneys[39] and in "distract[ing] directors" from core business decisions.[40] Finally, opponents of securities class action suits seek to tar the whole enterprise as a plaintiff attorney money-making machine.[41]

Indeed, these opponents have not sat idly by,[42] but have deployed several strategies over the years to try to impede federal securities class actions. First, these individuals turned to the courts. For instance, in a series of recent decisions, the Supreme Court has held that liability under the Securities Exchange Act of 1934 did not extend to "aiders and abettors"[43] and limited liability for individuals participating in a fraudulent scheme.[44]

Second, opponents of securities class actions have simultaneously turned to legislatures for redress. And Congress, in particular, has answered that call. Beginning in 1995 with the passage of the Private Securities Litigation Reform Act of 1995

---

[37] John C. Coffee, Jr., *Reforming the Securities Class Action: An Essay on Deterrence and Its Implementation*, 106 COLUM. L. REV. 1534, 1583 (2006).

[38] This "circularity argument" is one of the most contentious critiques of securities shareholder class actions, and proponents of such suits vociferously contest the point. *See, e.g.*, Lawrence E. Mitchell, *The "Innocent Shareholder": An Essay on Compensation and Deterrence in Securities Class-Action Lawsuits*, 2009 WIS. L. REV. 243, 244–45; Merritt B. Fox, *Why Civil Liability for Disclosure Violations When Issuers Do Not Trade?*, 2009 WIS. L. REV. 297, 303.

[39] *See* Andrew J. Pincus, What's Wrong with Securities Class Action Lawsuits? 3 (Feb. 5, 2014) (unpublished report) (on file with the U.S. Chamber Institute for Legal Reform), https://instituteforlegalreform.com/wp-content/uploads/2020/10/Securities_Class_Actions_Final1.pdf [https://perma.cc/BDV5-KPCT].

[40] Garry D. Hartlieb, *Enforceability of Mandatory Arbitration Clauses for Shareholder-Corporation Disputes*, 4 MICH. BUS. & ENTREPRENEURIAL L. REV. 131, 131 (2014).

[41] *See, e.g.*, *In re* Trulia, Inc. S'holder Litig., 129 A.3d 884, 891–92 (Del. Ch. 2016) (opining that class action shareholder actions "too often . . . serve[ ] only to generate fees for certain lawyers"); Scott, *supra* note 33.

[42] *See* Black, *supra* note 19, at 803 ("The attacks on the securities fraud class action never end.").

[43] Cent. Bank of Denver, N.A. v. First Interstate Bank of Denver, N.A., 511 U.S. 164, 188 (1994).

[44] *See* Stoneridge Inv. Partners, LLC v. Sci.-Atlanta, Inc., 552 U.S. 148, 166–67 (2008).

("PSLRA"),[45] Congress has capped damages,[46] excluded discovery before determinations on motions to dismiss,[47] and restricted access to state court for federal securities claims.[48] However, because of the mixed results from these efforts,[49] the discussion has turned to new strategies to eliminate such suits. Rather than relying on courts or Congress, opponents of securities class actions have now focused their efforts on private ordering.[50]

C. New Strategies

Of these private efforts, regulating litigation concerning the internal workings of a corporation has gained prominence among opponents of securities class actions. One such strategy practiced throughout the industry has been adding a forum selection bylaw.[51] A bylaw is an "administrative provision adopted by an organization," generally a corporation, that controls its internal governance.[52] In Delaware, the authority to adopt, repeal, or amend bylaws "shall be[long to] the stockholders"; however, stockholders may "confer th[is] power . . . upon the directors."[53] Further, a bylaw may not be "inconsistent with law or with the certificate of incorporation."[54]

In contrast, a forum selection clause concerns litigating disputes. Specifically, such a clause is a "contractual provision" designating an agreed-upon location—such as a country, state, or

---

[45] *See* Private Securities Litigation Reform Act of 1995, Pub. L. No. 104-67, 109 Stat. 737. PSLRA instituted a regime of "heightened pleading requirements, limits on damages and attorney's fees, a 'safe harbor' for certain kinds of statements, restrictions on the selection of lead plaintiffs in securities class actions, sanctions for frivolous litigation, and stays of discovery pending motions to dismiss." Halliburton Co. v. Erica P. John Fund, Inc., 573 U.S. 258, 277 (2014).

[46] *See* 15 U.S.C. § 78u-4(e) (2018).

[47] *See id.* § 78u-4(b)(3)(B).

[48] *See* Securities Litigation Uniform Standards Act of 1998, Pub. L. No. 105-353, § 16(b), 112 Stat. 3227, 3228.

[49] *See* Perino, *supra* note 28, at 915.

[50] *See* Christopher R. Drahozal, *Private Ordering and International Commercial Arbitration*, 113 PENN ST. L. REV. 1031, 1034 (2009) (defining private ordering as a system in which "non-governmental institution[s] . . . regulate the behavior of [their] members"); *see also* Omri Yadlin, *A Public Choice Approach to Private Ordering: Rent-Seeking at the World's First Futures Exchange*, 98 MICH. L. REV. 2620, 2620 (2000) (listing the varying definitions of private ordering).

[51] Joseph A. Grundfest & Kristen A. Savelle, *The Brouhaha over Intra-Corporate Forum Selection Provisions: A Legal, Economic, and Political Analysis*, 68 BUS. LAW. 325, 326 (2012).

[52] *Bylaw*, BLACK'S LAW DICTIONARY (11th ed. 2019).

[53] DEL. CODE ANN. tit. 8, § 109(a) (West 2015).

[54] *Id.* § 109(b).

type of court—to litigate disputes.[55] Advocates of these clauses assert that multi-jurisdictional litigation causes "[j]udicial resources [to be] wasted" as the "[d]efense counsel is forced to litigate the same case . . . in multiple courts."[56]

Recent decisions from Delaware courts have affirmed the enforceability of such bylaws regulating the internal workings of a corporation. First, in *Boilermakers Local 154 Retirement Fund v. Chevron Corp.*,[57] the chancery court upheld board-adopted forum selection bylaws[58] of both Chevron and FedEx.[59] In each case, the board adopted those bylaws without shareholder approval.[60] Then-Chancellor Strine found the challenged bylaws *did* affect the "rights" of current shareholders because they regulated "where stockholders can exercise their right to bring certain internal affairs claims."[61] The Chancery Court emphasized, however, that a newly promulgated bylaw must "relat[e] to the business of the corporation, the conduct of its affairs, and its rights or powers or the rights or powers of its stockholders, directors, officers or employees."[62]

---

[55] *Forum-Selection Clause*, BLACK'S LAW DICTIONARY (11th ed. 2019).

[56] *In re* Allion Healthcare Inc. S'holders Litig., No. 5022-CC, 2011 WL 1135016, at *4 (Del. Ch. Mar. 29, 2011); *see also* Joseph A. Grundfest, *The History and Evolution of Intra-Corporate Forum Selection Clauses: An Empirical Analysis*, 37 DEL. J. CORP. L. 333, 335 (2012) ("Forum selection clauses . . . reduce dispute resolution costs, promote efficient contracting, and enhance functional specialization in the judiciary.").

[57] 73 A.3d 934 (Del. Ch. 2013).

[58] *Id.* at 963. The full bylaw read:

> Unless the Corporation consents in writing to the selection of an alternative forum, the Court of Chancery of the State of Delaware shall be the sole and exclusive forum for (i) any derivative action or proceeding brought on behalf of the Corporation, (ii) any action asserting a claim of breach of a fiduciary duty owed by any director, officer or other employee of the Corporation to the Corporation or the Corporation's stockholders, (iii) any action asserting a claim arising pursuant to any provision of the Delaware General Corporation Law, or (iv) any action asserting a claim governed by the internal affairs doctrine. Any person or entity purchasing or otherwise acquiring any interest in shares of capital stock of the Corporation shall be deemed to have notice of and consented to the provisions of this [bylaw].

Id. at 942 (alteration in original).

[59] *Id.* at 937. The court consolidated shareholder challenges to both Chevron's and FedEx's forum selection bylaw because the provisions had the same language. *Id.* at 938.

[60] *Id.* at 938, 942.

[61] *Id.* at 951; *see also* Kevin M. LaCroix, *Delaware Chancery Court: Forum Selection Bylaw Valid*, D&O DIARY (June 25, 2013), https://www.dandodiary.com/2013/06/articles/shareholders-derivative-litigation/delaware-chancery-court-forum-selection-bylaw-valid/ [https://perma.cc/J92G-W99J].

[62] *Boilermakers Local 154 Ret. Fund*, 73 A.3d at 950.

Subsequently, the Delaware legislature codified the *Boilermakers* holding for forum selection clauses. As amended, section 115 of the Delaware General Corporation Law (DGCL) states:

> The 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. "Internal corporate claims" means claims, including claims in the right of the corporation, (i) that are based upon a violation of a duty by a current or former director or officer or stockholder in such capacity, or (ii) as to which this title confers jurisdiction upon the Court of Chancery.[63]

The new section authorizes forum selection clauses in the certificate of incorporation or bylaws that stipulate Delaware's Chancery Court as the exclusive forum for "internal corporate claims."[64] Put simply, Delaware corporations may now require all claims related to the corporation's internal affairs to be in Delaware state court. Also of note, the new legislation did not address federal securities claims.

Similar to *Boilermakers*, the Delaware Supreme Court, in *ATP Tour, Inc. v. Deutscher Tennis Bund*,[65] faced the enforceability of a unilaterally board-adopted fee-shifting bylaw of a non-stock corporation in cases of unsuccessful intra-corporate litigation.[66] Here, too, the Delaware Supreme Court held the bylaw was enforceable.[67] In coming to its conclusion, the court emphasized

---

[63] DEL. CODE ANN. tit. 8, § 115 (West 2015).

[64] *See* Jack B. Jacobs, *New DGCL Amendments Endorse Forum Selection Clauses and Prohibit Fee-Shifting*, HARV. L. SCH. F. ON CORP. GOVERNANCE (June 17, 2015), https://corpgov.law.harvard.edu/2015/06/17/new-dgcl-amendments-endorse-forum-selection-clauses-and-prohibit-fee-shifting/ [https://perma.cc/3NBA-D2RW].

[65] 91 A.3d 554 (Del. 2014). The case had been certified to the Delaware Supreme Court by the Delaware Federal District Court. *Id.* at 555.

[66] *Id.* at 556.

[67] *Id.* at 560. Due to a public outcry in response to the decision, the Delaware legislature amended current law to prevent fee-shifting bylaws. *See* tit. 8, § 102(f) ("The certificate of incorporation may not contain any provision that would impose liability on a stockholder for the attorneys' fees or expenses of the corporation or any other party in connection with an internal corporate claim, as defined in § 115 of this title."); *see also* DEL. CORP. L. COUNCIL, EXPLANATION OF COUNCIL LEGISLATIVE PROPOSAL 3–4 (Mar. 6, 2015), https://www.corporatedefensedisputes.com/wp-content/uploads/sites/19/2015/03/COUNCIL-SECOND-PROPOSAL-EXPLANATORY-PAPER-3-6-15-U0124513.pdf [https://perma.cc/92Y8-JKDL] (fearing that "[f]ee-[s]hifting [p]rovisions [w]ill [m]ake [s]tockholder [l]itigation, [e]ven if [m]eritorious, [u]ntenable").

the fact that fee-shifting only occurred within the context of "intra-corporate litigation."[68] In other words, the Court found the bylaw merely allocated risk among intra-corporate parties, which, to the court, tracked the mandates of title 8, section 109(b), of the Delaware Code.[69]

Although not dealing with federal securities claims, these recent decisions by Delaware courts have helped clarify the lengths, and limits, parties can go through for private ordering. The courts' holdings in *ATP Tour, Inc.* and *Boilermakers* suggest that boards have near-unfettered discretion when operating within internal affairs.[70] Yet these two decisions also suggest that the board's authority does not reach outside that sphere.

Buoyed by the success of expansive bylaws regulating corporate internal affairs,[71] opponents of shareholder class action claims have trained their eyes on a new frontier: arbitration[72] bylaws regulating federal securities claims. To this point, the wisdom, and more importantly the enforceability, of such arbitration bylaws has been questioned by scholars and the SEC.[73] And even the most ardent supporters of forum selection bylaws have recog-

---

[68] *ATP Tour, Inc.*, 91 A.3d at 557. Later, in *Salzberg v. Sciabacucchi*, the Delaware Supreme Court drew a distinction between intra-corporate and internal-affairs claims. 227 A.3d 102, 130–31 (Del. 2020). Although not the focus of this paper, this decision is briefly discussed *infra* notes 126–152 and accompanying text.

[69] *ATP Tour, Inc.*, 91 A.3d. at 558.

[70] In the four months immediately following the *Boilermakers* decision, 112 Delaware Corporations adopted or announced plans to adopt exclusive forum bylaws. *See* Claudia H. Allen, *United States: Trends in Exclusive Forum Bylaws*, MONDAQ (Jan. 22, 2014), http://www.mondaq.com/unitedstates/x/287660/Shareholders/Trends+In+Exclusive+Forum+Bylaws [https://perma.cc/9JJH-R4LG].

[71] *See id.*; *see also, e.g.*, Boilermakers Local 154 Ret. Fund v. Chevron Corp., 73 A.3d 934, 963 (Del. Ch. 2013); City of Providence v. First Citizens BancShares, Inc., 99 A.3d 229, 230, 242 (Del. Ch. 2014) (upholding a bylaw selecting the federal Eastern District of North Carolina as the designated forum). *But see* Galaviz v. Berg, 763 F. Supp. 2d 1170, 1175 (N.D. Cal. 2011) (finding that a forum selection bylaw unilaterally adopted by corporate directors is unenforceable).

[72] An arbitration clause is an agreement between contracting parties to settle disagreements through a "dispute-resolution process" overseen by "one or more neutral third parties." *Arbitration*, BLACK'S LAW DICTIONARY (11th ed. 2019); *see also* Dep't of Transp. v. Pub. Citizen, 541 U.S. 752, 760 (2004) (describing arbitration as a "dispute-resolution process").

[73] *See supra* note 19 and accompanying text; Hogan Lovells US LLP, SEC No-Action Letter, *supra* note 12; Lawrence A. Hamermesh, *Delaware Law Status of Bylaws Regulating Litigation of Federal Securities Law Claims*, HARV. L. SCH. F. ON CORP. GOVERNANCE (Nov. 29, 2018), https://corpgov.law.harvard.edu/2018/11/29/delaware-law-status-of-bylaws-regulating-litigation-of-federal-securities-law-claims [https://perma.cc/76FP-853R].

nized arbitration bylaws raise different enforceability questions.[74] Nonetheless, parties have proceeded with arbitration bylaw proposals, such as the Doris Behr 2012 Irrevocable Trust and the trustee of Commonwealth REIT.[75] Others have backed off proposals after opposition from the SEC, like the proposals from both Gannett and Pfizer[76] and one by the Carlyle Group L.P. in 2012.[77]

While much of the scholarship in this area has focused on the preemptive effect of the Federal Arbitration Act,[78] not enough attention has been paid to whether such bylaws are allowed in the first place under state-corporate law. Even those articles that have made a corporation's internal affairs the central theme have only briefly discussed the doctrine's applicability to arbitration clauses.[79]

Yet, even absent exhaustive scholarship, the uncertainty demonstrated by scholars and the SEC about enforceability of arbitration bylaws is unsurprising as such clauses raise serious state law concerns. In particular, such arbitration bylaws clash with traditional notions of corporate internal affairs.

II. THE LIMITATIONS ON PRIVATE ORDERING IMPOSED BY THE INTERNAL AFFAIRS DOCTRINE

Arbitration bylaws seeking to cover disputes involving federal securities transactions do not satisfy the requirements of the internal affairs doctrine. First, federal securities claims are unconcerned with the relationship between the corporation, directors, and stockholders. Indeed, many securities transactions occur between a corporation and a then-third party. Thus, such transactions do not implicate the internal affairs of a corporation. Moreover, long-standing precedent by legislatures

---

[74] *See, e.g.*, Joseph A. Grundfest, *The Limits of Delaware Corporate Law: Internal Affairs, Federal Forum Provisions, and* Sciabacucchi, 75 BUS. LAW. 1319, 1331 (2020).

[75] *See supra* Introduction.

[76] *See supra* note 12 and accompanying text.

[77] "[T]he SEC effectively blocked the IPO" of the Carlyle Group L.P. after the company had intended to include an arbitration clause for federal securities claims in its originating documents. Andrew Rhys Davies, *Should the SEC Allow IPOs When Bylaws Require Arbitration of Federal Securities Claims?*, N.Y. L.J. (July 26, 2018, 2:30 PM), https://www.law.com/newyorklawjournal/2018/07/26/should-the-sec-allow-ipos-when-bylaws-require-arbitration-of-federal-securities-claims/ [https://perma.cc/NT66-FFL2].

[78] *See supra* note 19 and accompanying text.

[79] *See generally, e.g.*, Mohsen Manesh, *The Contested Edges of Internal Affairs*, 87 TENN. L. REV. 251, 295–96 (2020).

and courts has sought to bifurcate claims over a corporation's internal affairs and the federal securities laws.

A. The Doctrine

Recent decisions by Delaware courts on the reach of corporations' governance documents rest on the internal affairs doctrine. The internal affairs doctrine revolves around internal corporate governance, usually expressed through documents such as bylaws and charters.[80] Specifically, the doctrine is a choice of law principle.[81] This distinction between internal and external affairs comes from corporate governance being within the province of state law in the United States.[82] To remedy any confusion that may stem from potentially fifty sets of corporate law, the internal affairs doctrine ensures "that only one State should have the authority to regulate a corporation's . . . affairs" for the corporation to avoid "conflicting demands."[83] Thus, the state law in which incorporation occurred controls over disputes arising from the corporation's internal affairs.[84] While most states have codified

---

[80] *See* Henry DuPont Ridgely, *The Emerging Role of Bylaws in Corporate Governance*, 68 SMU L. REV. 317, 318–19 (2015); 1 WILLIAM BLACKSTONE, COMMENTARIES *475–76 ("[B]y-laws or private statutes [are] for the better government of the corporation . . . .").

[81] *See* Richard M. Buxbaum, *The Threatened Constitutionalization of the Internal Affairs Doctrine in Corporation Law*, 75 CALIF. L. REV. 29, 44 (1987); Frederick Tung, *Before Competition: Origins of the Internal Affairs Doctrine*, 32 J. CORP. L. 33, 39 (2006) ("In its modern form, the internal affairs doctrine is a choice of law rule, widely accepted among states . . . ."); VantagePoint Venture Partners 1996 v. Examen, Inc., 871 A.2d 1108, 1112 (Del. 2005) ("The internal affairs doctrine is a long-standing choice of law principle which recognizes that only one state should have the authority to regulate a corporation's internal affairs—the state of incorporation.").

[82] *See* Kamen v. Kemper Fin. Servs., Inc., 500 U.S. 90, 98 (1991) (describing corporate governance litigation as involving "private parties hav[ing] entered legal relationships with the expectation that their rights and obligations would be governed by state-law standards"); Santa Fe Indus., Inc. v. Green, 430 U.S. 462, 479 (1977) ("Corporations are creatures of state law . . . ." (quoting Cort v. Ash, 422 U.S. 66, 84 (1975))).

[83] Edgar v. MITE Corp., 457 U.S. 624, 645 (1982); *see also* Manesh, *supra* note 79, at 263–64.

[84] Lynn M. LoPucki, *Corporate Charter Competition*, 102 MINN. L. REV. 2101, 2110 (2018).

the internal affairs doctrine,[85] some scholars and judges believe that the doctrine is a constitutional command.[86]

To abide by this choice of law principle, a corporation's bylaws must relate to "the business of the corporation[ ], the conduct of [its] affairs, or the rights of the stockholders."[87] Further, valid bylaws must be "procedural [and] process-oriented [in] nature"[88] in that they "direct how the corporation, the board, and its stockholders may take certain actions."[89] Put differently, the internal affairs doctrine distinguishes between actions by an individual or a corporation and actions "peculiar to the corporate entity."[90]

As a general matter, the exact reach of the doctrine remains an open question.[91] While courts—especially Delaware courts—have taken an expansive view of the internal affairs doctrine,[92] these outcomes have done little to establish the exact contours of the doctrine. In fact, courts within the same state will often have conflicting holdings on the same issue concerning the reach of the

---

[85] *See, e.g.*, DEL. CODE ANN. tit. 8, § 109(b) (West 2015) ("The bylaws may contain any provision . . . relating to the business of the corporation, the conduct of its affairs, and its rights or powers or the rights or powers of its stockholders, directors, officers or employees."); MODEL BUS. CORP. ACT § 15.01(a) (AM. BAR ASS'N 2017) ("The law of the jurisdiction of formation of a foreign corporation governs . . . the internal affairs of the foreign corporation . . . .").

[86] Buxbaum, *supra* note 81, at 44 (claiming the internal affairs doctrine is rooted in the Fair Faith and Credit Clause); McDermott Inc. v. Lewis, 531 A.2d 206, 217 (Del. 1987) ("[W]e conclude that application of the internal affairs doctrine is mandated by constitutional principles . . . ."). *But see* Larry E. Ribstein & Erin Ann O'Hara, *Corporations and the Market for Law*, 2008 U. ILL. L. REV. 661, 716 ("[T]he [internal affairs doctrine] never has been entitled to constitutional protection . . . .").

[87] Boilermakers Local 154 Ret. Fund v. Chevron Corp., 73 A.3d 934, 951 (Del. Ch. 2013); *see also Edgar*, 457 U.S. at 645–46.

[88] *Boilermakers Local 154 Ret. Fund*, 73 A.3d at 951 (quoting CA, Inc. v. AFSCME Emps. Pension Plan, 953 A.2d 227, 235 (Del. 2008)).

[89] *Id.*

[90] *McDermott Inc.*, 531 A.2d at 214; *accord* Salzberg v. Sciabacucchi, 227 A.3d 102, 128 (Del. 2020).

[91] *See* Jill E. Fisch & Steven Davidoff Solomon, Centros*, California's "Women on Boards" Statute and the Scope of Regulatory Competition* 8 (Eur. Corp. Governance Inst., Law Working Paper No. 454/2019, 2019), https://papers.ssrn.com/sol3/papers.cfm?abstract_id=3384768 ("[T]he scope of the internal affairs doctrine . . . remain[s] somewhat unclear.").

[92] *See* Manesh *supra* note 79, at 269; *see also* VantagePoint Venture Partners 1996 v. Examen, Inc., 871 A.2d 1108, 1113 (Del. 2005) ("[T]he conflicts practice of both state and federal courts has consistently been to apply the law of the state of incorporation to '*the entire gamut* of internal corporate affairs.' " (emphasis added) (quoting *McDermott Inc.*, 531 A.2d at 216)). This capacious reading of the internal affairs doctrine by Delaware courts should come as no surprise because, considering that the majority of corporations incorporate in Delaware, such rulings enlarge the power of its state courts. *See* Manesh *supra* note 79, at 269.

internal affairs doctrine.[93] Given this uncertainty, the recent decisions from Delaware Courts[94] help clarify the doctrine.

B. Internal Affairs and Federal Securities Transactions

Past practices of legislatures and courts of separating internal corporate matters and federal securities laws clash with the legal scheme envisioned by advocates of arbitration bylaws. In fact, the bifurcation of securities transactions and corporate internal affairs dates back to some of the oldest cases in this field.[95] Congress has also supported the division of federal and state law concerning corporations. Recognizing the long-standing principle of avoiding the overlap between federal securities law and state corporate law, Congress added a "savings clause"—known as the "Delaware carve-out"[96]—to the Securities Litigation Uniform Standards Act of 1998 ("SLUSA")[97] to "preserve[ ] certain types of state-law claims that would otherwise be subject to its preclusion provision."[98] To that end, SLUSA's legislative history buttresses the claim that Congress was concerned with avoiding overlap.[99]

---

[93] *Compare* Miesse v. Seiberling Rubber Co., 264 A.D. 373, 374 (1st Dep't 1942) (finding a dispute over redeeming preferred stock under the corporation's internal affairs), *with* Borst v. E. Coast Shipyards, 105 N.Y.S.2d 228, 231–32 (Sup. Ct. N.Y. Cnty. 1951) (holding the plaintiff's claim to redeem preferred stock was not a matter under the internal affairs doctrine).

[94] *See supra* notes 57–71 and accompanying text.

[95] *See, e.g.*, Williams v. Gaylord, 186 U.S. 157, 165 (1902) ("[W]hen a corporation sells or encumbers its property, incurs debts or gives securities, it does business, and a statute regulating such transactions does not regulate the internal affairs of the corporation.").

[96] Kenneth Hsu, *The Delaware Carve-Out's Carve: Examining and Repairing SLUSA's State Law Exception*, 11 HASTINGS BUS. L.J. 385, 387 (2015).

[97] Securities Litigation Uniform Standards Act of 1998, Pub. L. No. 105-353, 112 Stat. 3227. Congress has also sought to create corporate carve outs in other areas of the law. *See, e.g.*, 28 U.S.C. § 1332(d)(9)(C) (2018) (exempting certain internal affairs claims from the Class Action Fairness Act of 2005).

[98] Madden v. Cowen & Co., 576 F.3d 957, 964 (9th Cir. 2009); *see also* Malone v. Brincat, 722 A.2d 5, 13 (Del. 1998) ("The 1998 Act, however, contains two important exceptions . . . . These exceptions have become known as the 'Delaware carve-outs.' ").

[99] The Senate Committee Report on SLUSA states, in part:

> The Committee is keenly aware of the importance of state corporate law, specifically those states that have laws that establish a fiduciary duty of disclosure. It is not the intent of the Committee in adopting this legislation to interfere with state law regarding the duties and performance of an issuer's directors or officers in connection with a purchase or sale of securities by the issuer or an affiliate from current shareholders or communicating with existing shareholders with respect to voting their shares, acting in response to a tender or exchange offer, or exercising dissenters' or appraisal rights.

S. REP. NO. 105-182, at 6 (1998).

Courts, too, have been wary of allowing the legal scheme advanced by arbitration bylaw advocates. In particular, the Supreme Court has explicitly rejected attempts to "federalize"[100] causes of action dealing with a corporation's internal workings. For instance, in *Santa Fe Industries, Inc. v. Green*, the Court refused to adopt a " 'federal fiduciary principle' under Rule 10b-5."[101] In coming to its holding, the Court relied on congressional intent in enacting the Securities Exchange Act, which "did not seek to regulate transactions which constitute[d] . . . internal corporate mismanagement."[102] Instead, the 1934 Act sought to regulate transactions between outside third parties.[103]

Yet more problematic for advocates of arbitration bylaws is the Supreme Court's holding in *Edgar v. MITE Corp.*, which struck down the Illinois Business Take-Over Act as an impermissible burden on interstate commerce.[104] The Illinois Act, applying to issuers of securities "of which shareholders located in Illinois own 10%," regulated tender offers.[105]

In rejecting the argument that the Illinois statute regulated internal affairs, Justice White, writing for the Court, defined tender offers as "transfers of stock by stockholders to a third party [that] do not themselves implicate the internal affairs of the target company."[106] Under this definition, the court found that tender offers involve a then-third party and that they thus have no bearing on the internal rights of the transacting corporation.[107]

---

[100] Santa Fe Indus., Inc. v. Green, 430 U.S. 462, 479 (1977) ("Absent a clear indication of congressional intent, we are reluctant to federalize the substantial portion of the law of corporations that deals with transactions in securities, particularly where established state policies of corporate regulation would be overridden."); *see also* Bus. Roundtable v. SEC, 905 F.2d 406, 412–13 (D.C. Cir. 1990) (finding the newly promulgated SEC rule requiring corporations to abide by one share/one vote principles to be a federal intrusion into a "major issue[ ] traditionally governed by state law").

[101] *Santa Fe Indus.*, 430 U.S. at 479.

[102] *Id.* (quoting Superintendent of Ins. v. Bankers Life & Cas. Co., 404 U.S. 6, 12 (1971)).

[103] *Superintendent of Ins.*, 404 U.S. at 12.

[104] Edgar v. MITE Corp., 457 U.S. 624, 646 (1982).

[105] *Id.* at 627.

[106] *Id.* at 645.

[107] *Id.* As with securities transactions generally, the buyer—in this case the tender offeror—may already own other shares of the company, but that is irrelevant to the role it occupies as to the transaction at issue. Federal Securities laws apply equally to current-shareholders and non-shareholders alike. Further, these laws are only concerned with the effect of potential violations of its provisions on an investor acting in that role as to that *particular transaction*. Any other relationship to the company, as to the transaction, is irrelevant.

With this precedential background from the Supreme Court, and recent holdings from Delaware Courts, it is hard to imagine a scenario where arbitration bylaws seeking to cover federal securities transactions would fall within the internal affairs of a corporation. If tender offers do not regulate a corporation's internal affairs, how do standard market transactions affect internal affairs? To that end, as the Chancery Court stated in *Sciabacucchi*, "the purchaser is not yet a stockholder and does not yet have any relationship with the corporation that is governed by Delaware corporate law."[108] While the purchaser of stock will *eventually* become associated with the interplay of the rights and powers between the corporation, directors, and stockholders, at the time of purchase he or she is an outside third party. No amount of clever argumentation can explain away the inclusion of a then-third party under a doctrine that only touches matters "*peculiar* to [the] corporation[ ]."[109]

What is more, federal securities claims implicate different rights than those under a corporation's internal affairs.[110] A corporation is brought into existence by the state as a sovereign power, which governs the corporation through the state's operative law.[111] Through this process, state law reigns over the internal determinations of the corporation.[112] By contrast, federal securities transactions derive from federal law meant to regulate the purchase and sale of securities. A securities claim thus implicates a violation of federal law at most incidental to the internal workings of a corporation. Simply put, the state-based rights of the internal affairs doctrine are unconcerned whether parties follow federal law.

Indeed, federal securities transactions conflict with the long-held understanding by Delaware Courts of a corporation's internal affairs. Federal securities transactions do not "pertain to the relationships among or between the corporation and its officers,

---

[108] Sciabacucchi v. Salzberg, No. 2017-0931, 2018 WL 6719718, at *17 (Del. Ch. Dec. 19, 2018), *rev'd,* 227 A.3d 102 (Del. 2020).

[109] QVT Fund LP v. Eurohypo Cap. Funding LLC I, No. 5881, 2011 WL 2672092, at *7 (Del. Ch. July 8, 2011) (quoting McDermott Inc. v. Lewis, 531 A.2d 206, 215 (Del. 1987)).

[110] *See* Roberta S. Karmel, *Realizing the Dream of William O. Douglas—The Securities and Exchange Commission Takes Charge of Corporate Governance*, 30 DEL. J. CORP. L. 79, 80 (2005) ("The federal securities laws generally have been considered full disclosure statutes, as opposed to merit regulation statutes or laws governing the internal affairs of corporations.").

[111] *See Sciabacucchi*, 2018 WL 6719718, at *18.

[112] *See supra* note 81 and accompanying text.

directors, and shareholders."[113] As securities transactions occur by an outside, third party, the transaction is not "among or between" the internal affair's stakeholders.[114] While engaging in securities transactions are acts corporations participate in, courts must exclude from the internal affairs doctrine "acts which can be performed by both corporations and individuals."[115] That is why the internal affairs doctrine "does not extend to claims 'where the rights of third parties external to the corporation are at issue.' "[116]

Other claims that do fall within a corporation's internal affairs are illustrative of the disconnect between such a claim and federal securities transactions. For instance, the internal affairs doctrine implicates disputes over whether a contract binds a corporation created in a "spin-off transaction" that the former parent company engaged in with its former stockholder.[117] Putting aside the more esoteric contract questions, the issue for the stockholders involved the internal affairs doctrine because the relevant terms of the agreement pertained to the rights of stockholders with the corporation. Unlike the position of the buyer in many securities transactions, the plaintiffs here were stockholders *at the time* the deal was struck. Nor is a dispute over a contractual "put right"[118] clause, that gave the plaintiff the authority to dissolve the company, outside the reach of the internal affairs doctrine.[119] Dissimilar to a federal securities claim, which stems from federal law, the ability to dissolve a company directly

---

[113] VantagePoint Venture Partners 1996 v. Examen, Inc., 871 A.2d 1108, 1113 (Del. 2005).

[114] *See* Citigroup Inc. v. AHW Inv. P'ship, 140 A.3d 1125, 1140 (Del. 2016) (holding that a defendant's misstatement about a stock trade resulted in a "personal" claim that was not "governed by the internal affairs doctrine"); *see also In re* Ebix, Inc. S'holder Litig., No. 8526-VCN, 2014 WL 3696655, at *17 (Del. Ch. July 24, 2014) (explaining that "this Court does not have subject matter jurisdiction" over "issue[s] . . . governed by the federal securities laws").

[115] McDermott Inc. v. Lewis, 531 A.2d 206, 214 (Del. 1987).

[116] Stewart v. Wilmington Tr. SP Servs., Inc., 112 A.3d 271, 291 (Del. Ch.) (quoting VantagePoint Venture Partners 1996, 871 A.2d at 1113 n.14), *aff'd,* 126 A.3d 1115 (Del. 2015).

[117] *See* Miramar Police Officers' Ret. Plan v. Murdoch, No. 9860, 2015 WL 1593745, at *1 (Del. Ch. Apr. 7, 2015).

[118] JOHN B. LYNCH, JR. & TAYLOR A. SHEA, A PRACTICAL GUIDE TO ORGANIZING A BUSINESS IN CONNECTICUT § 7.8.2 ("A put right gives a stakeholder the right to force the company and/or other stakeholders (in proportion to their ownership interests) to purchase from it all of its interest in the company under certain specified circumstances.").

[119] *See* Terramar Retail Ctrs., LLC v. Marion #2-Seaport Tr., No. 12875, 2017 WL 3575712, at *1–3 (Del. Ch. Aug. 18, 2017), *aff'd*, 184 A.3d 1290 (Del. 2018).

implicates the rights derived from one's legal relationship with the company.

Proponents of a broad reading of the internal affairs doctrine proffer that securities laws are "clearly internal" because of the internal nature of board decisions that give rise to the securities claim.[120] But such a view misreads the internal affairs doctrine—especially after *Boilermakers* and *ATP Tour, Inc.*—and would lead to confusing results. Indeed, such an everything-between-the-shareholders-and-company-is-internal-affairs approach has no logical end. What happens if a director, furious at a stockholder over a recent proxy vote, assaulted the stockholder on the company's premises? This example involves the directors, company, and stockholders but does not fall within the internal affairs doctrine.

But more problematic for this reading of the internal affairs doctrine is that myriad claims once excluded from a corporation's internal affairs would now find such a home. For instance, creditors of an insolvent corporation, seeking to bring the suit under Delaware law, could now justifiably make such a claim.[121] Likewise, claims against aiders and abettors of a director's breach of fiduciary duty in a merger could be under the corporation's internal affairs.[122] In fact, the latter example parallels federal securities claims because both involve the purchase of a corporation's shares. Put succinctly, these claims are not predicated on the relationship between stockholders, directors, and the corporation, as required by the internal affairs doctrine,[123] but rather on relationships of outsiders to these three stakeholders.

It is against this traditional legal backdrop, with the requirement that a corporation's bylaws or charter provisions involve issues that touch upon a relationship peculiar to the stockholders, directors, and the corporation, in which most state laws are passed.[124] Indeed, the Delaware legislature recently codified the

---

[120] *See, e.g.*, Grundfest, *supra* note 74, at 1364.

[121] *Cf.* Askanase v. Fatjo, 130 F.3d 657, 670–71 (5th Cir. 1997) (holding claims by a trustee of an insolvent corporation against creditors for improper transfer of corporate funds were not a matter under the corporation's internal affairs so Texas law, rather than Delaware law, governed).

[122] *Cf.* Dominion Energy, Inc. v. City of Warren Police & Fire Ret. Sys., 928 F.3d 325, 337 (4th Cir. 2019) (finding claims by former shareholders of a merged corporation against the directors of the acquirer corporation for aiding and abetting a breach of fiduciary duty were outside the corporation's internal affairs).

[123] *See supra* notes 80–109 and accompanying text.

[124] *See, e.g.*, NEB. REV. STAT. ANN. § 21-2,207(c) (West 2017) ("The Nebraska Model Business Corporation Act does not authorize this state to regulate the

Boilermakers's decision, thus solidifying the rule that corporations may not enact forum selection clauses that govern external claims.[125] It was for these reasons that the Delaware Supreme Court's holding in *Salzberg v. Sciabacucchi*, overturning the Chancery Court,[126] was so puzzling.

The Delaware Chancery had invalidated forum selection clauses in three companies' initial public offerings[127] that required claims under the Securities Act of 1933 to be filed in federal court.[128] In reversing the Chancery's decision, the Delaware Supreme Court held that, while not within a corporation's internal affairs,[129] federal securities laws are within "intra-corporate" affairs.[130] This term, explained the court, described an area in

---

organization or internal affairs of a foreign corporation authorized to transact business in this state."); ARK. CODE ANN. § 4-28-604 cmt. 2 (West 2012) ("This Act's applicability to UNAs formed in other jurisdictions that are operating in this state is necessary because in all other types of entities the internal affairs rules of the jurisdiction of the entity's formation (e.g., the governance rules and duties and responsibilities of the owners and managers to each other and the entity) control . . . .").

[125] *See supra* notes 62–63 and accompanying text.

[126] 227 A.3d 102, 109 (Del. 2020).

[127] The three companies were Blue Apron, Stitch Fix, and Roku. *See* Kevin M. LaCroix, *Delaware Court Holds Charter Provision Designating a Federal Forum for Section 11 Claims Is Invalid*, D&O DIARY (Dec. 19, 2018), https://www.dandodiary.com/2018/12/articles/securities-litigation/delaware-court-holds-charter-provision-designating-federal-forum-section-11-claims-invalid/ [https://perma.cc/WE4B-MC7T]. Roku's and Stitch Fix's forum selection provision reads:

> Unless the Company consents in writing to the selection of an alternative forum, the federal district courts of the United States of America shall be the exclusive forum for the resolution of any complaint asserting a cause of action arising under the Securities Act of 1933. Any person or entity purchasing or otherwise acquiring any interest in any security of the Corporation shall be deemed to have notice of and consented to [this provision].

Sciabacucchi v. Salzberg, No. 2017-0931, 2018 WL 6719718, at *6 (Del. Ch. Dec. 19, 2018) (alteration in the original), *rev'd*, 227 A.3d 102 (Del. 2020).

[128] *Sciabacucchi*, 2018 WL 6719718, at *1.

[129] *Salzberg*, 227 A.3d at 123 ("[N]ot even Appellants are contending that Section 11 claims are 'internal affairs' claims . . . .").

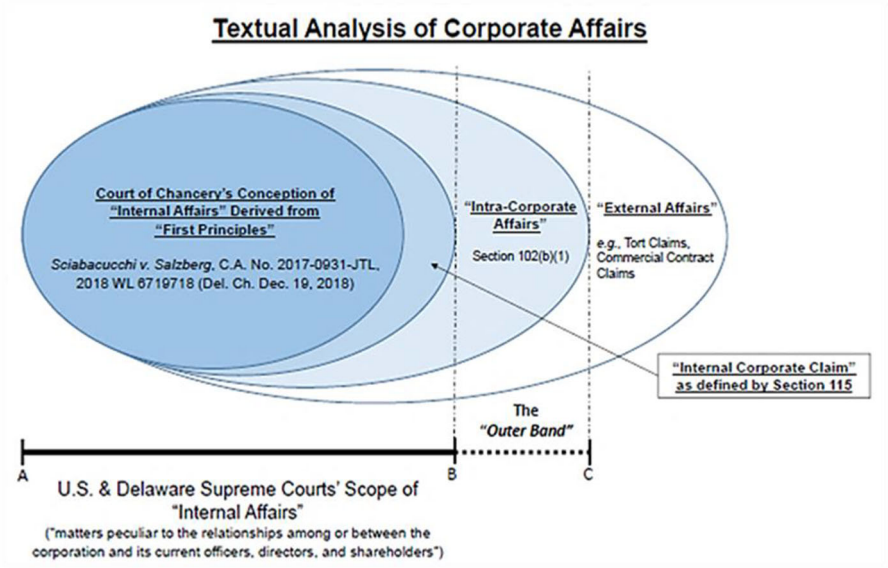
[130] *Id.* at 125.

between a corporation's internal and external affairs.[131] And title 8, section 102(b)(1), of the Delaware Code, which does not mention internal affairs, authorized purportedly intra-corporate actions.[132]

This dichotomy between internal and intra-corporate affairs is novel, however.[133] Oddly enough, in the court's attempt to define "intra-corporate affairs," it cited cases that used "intracorporate" and "internal" disputes interchangeably as well as scholarly work on the definition of the internal affairs doctrine.[134] Nevertheless, the Delaware Supreme Court, in essence, adopted the position offered by the petitioner at oral argument: "If the legislatures wanted to say internal affairs, they knew how to say it."[135]

---

[131] To illustrate the point, the court created a Venn diagram:



Id. at 131 fig.1.

[132] *Id.* at 131. Of note for this paper, the Delaware Supreme Court found that Delaware law forbids corporations from including mandatory arbitration provisions in their certificate of incorporation or bylaws under the plain language of title 8, section 115, of the Delaware Code. *Id.* at 137 n.169.

[133] While addressing the topics briefly, this paper does not take a deep dive into *Salzberg v. Sciabacucchi* or this new intra-corporate affairs theory.

[134] *See, e.g.*, *Salzberg*, 227 A.3d at 128 (quoting McDermott Inc. v. Lewis, 531 A.2d 206, 216 (Del. 1987) (internal citation omitted)); *id.* at 125 n.99 (citing Manesh, *supra* note 79, at 297–98); *see also* Ann Lipton, *So the* Salzberg v. Sciabacucchi *Decision Is In!*, BUS. L. PROF BLOG (Mar. 21, 2020), https://lawprofessors.typepad.com/business_law/2020/03/so-the-salzberg-v-sciabacucchi-decision-is-in.html [https://perma.cc/H5FR-WHKS] (making the same point).

[135] Oral Argument at 11:45, *Salzberg*, 227 A.3d 102 (Del. 2020) (No. 346,2019), https://livestream.com/accounts/5969852/events/8952021/videos/200564724/player.

Yet this argument turns accepted principles of statutory interpretation on their head. While the Delaware Supreme Court claimed its only job was to "construe the plain language of the statute,"[136] no other federal or state court has adopted the position that laws are passed "upon a clean slate."[137] Instead, legislatures are understood to pass laws "against a background" of "common-law principle[s],"[138] which informs the statutory language. For instance, courts have held that congress writes bankruptcy laws in the context of the "pre-Code rule[s],"[139] that the Federal Rules of Evidence are drafted with the "prevailing common-law rule[s]" in mind,[140] and that criminal laws are passed against the backdrop of "the deep-rooted nature of law-enforcement discretion . . . ."[141]

Under this framework, accepted by numerous different fields of law, the Delaware legislature would be expected to make a clear statement if it wished *not* to be bound by the internal affairs doctrine.[142] Otherwise, it should be presumed that the legislature was acting within the "hundred years"[143] old guidelines of this doctrine.[144] In fact, then-Chancellor Strine's opinion in *Boiler-*

---

[136] *Salzberg*, 227 A.3d at 125.

[137] Oubre v. Entergy Operations, Inc., 522 U.S. 422, 435 (1998) (Thomas, J., dissenting).

[138] Astoria Fed. Sav. & Loan Ass'n v. Solimino, 501 U.S. 104, 108 (1991); *accord* Mountain Peaks Fin. Servs., Inc. v. Roth-Steffen, 778 N.W.2d 380, 384 (Minn. Ct. App. 2010); Scott v. Mattingly, 488 N.W.2d 349, 352 (Neb. 1992); *cf.* Note, *The Internal Affairs Doctrine: Theoretical Justifications and Tentative Explanations for Its Continued Primacy*, 115 HARV. L. REV. 1480, 1482 (2002) (describing the internal affairs doctrine as "customary common law"); Oral Argument at 21:27, *Salzberg*, 227 A.3d 102 (Del. 2020) (No. 346,2019), https://livestream.com/accounts/5969852/events/8952021/videos/200564724/player (acknowledging that the internal affairs doctrine is "a part of [Delaware's] common law").

[139] *E.g.*, Dewsnup v. Timm, 502 U.S. 410, 417 (1992).

[140] *E.g.*, Tome v. United States, 513 U.S. 150, 156 (1995).

[141] *E.g.*, Town of Castle Rock v. Gonzales, 545 U.S. 748, 761 (2005) (Scalia, J.). Justice Scalia's opinion is noteworthy because even he, a leader in the move to enshrine "textualism" as the primary statutory-interpretive tool of the judiciary, *see* Paul Clement, *Arguing Before Justice Scalia*, N.Y. TIMES (Feb. 17, 2016), https://www.nytimes.com/2016/02/17/opinion/arguing-before-justice-scalia.html [https://perma.cc/EHZ6-VPFD], never claimed that the text of the statute was the *only* acceptable consideration for the court.

[142] *Cf. Salzberg*, 227 A.3d at 125 (Del. 2020) ("If our General Assembly wishes to narrow the scope of Section 102(b)(1) to be aligned perfectly with the boundaries of the internal affairs doctrine, it could do so.").

[143] Oral Argument at 21:17, *Salzberg*, 227 A.3d 102 (Del. 2020) (No. 346,2019), https://livestream.com/accounts/5969852/events/8952021/videos/200564724/player.

[144] *Cf.* Hamilton v. United Laundries Corp., 111 N.J. Eq. 78, 80 (N.J. Ch. 1932) (explaining that it "is almost too obvious for remark that [the state of New Jersey] cannot regulate the internal affairs of foreign corporations" (quoting Gregory v. N.Y., Lake Erie & W. R.R. Co., 40 N.J. Eq. 38, 44 (N.J. Ch. 1885))). The Delaware Supreme

makers Local 154 Retirement Fund v. Chevron Corp.[145] appeared to proceed under this framework. This is because although Delaware's statute for bylaws, title 8, section 109(b), of the Delaware Code, did not explicitly mention a corporation's internal affairs,[146] the opinion still explained how bylaws regulating "external matters" would be unenforceable.[147]

At bottom, the Delaware Supreme Court's decision has created "uncertain challenges"[148] for corporate law moving forward. Is there, for instance, a different analysis for Section 11 claims and those under 10b-5?[149] And how will *Salzberg* impact decisions by other states' highest courts on the limits of their corporate law,[150] as other states "often look[ ] to Delaware's rich abundance of corporate law for guidance"?[151] Based on the preceding sections, these state courts should try to stay in their "lane[s]" by maintaining the traditional limits on corporate authority that were universally

---

Court made much of the fact that the Delaware legislature explicitly mentions "internal affairs" in other statutes, *see Salzberg*, 227 A.3d at 117–19, but it is unclear why that changed the analysis. There is no support for the proposition that a legislature explicitly mentioning a common-law principle in the text of a statute vitiates for the remaining laws within the jurisdiction the accepted statutory interpretive rule that laws are passed against the backdrop of common-law principles.

[145] Boilermakers Local 154 Ret. Fund v. Chevron Corp., 73 A.3d 934, 952 (Del. Ch. 2013).

[146] It instead constrained a corporation's bylaws to "the business of the corporation, the conduct of its affairs, and . . . the rights or powers of its stockholders, directors, officers or employees." *Id.* (alteration in original) (quoting DEL. CODE ANN. tit. 8 § 109(b) (West 2015)); *cf.* DEL. CODE ANN. tit. 8 § 102(b)(1) (West 2018) ("Any provision for the management of the business and for the conduct of the affairs of the corporation, and . . . regulating the powers of the corporation, the directors, and the stockholders, or any class of the stockholders, or the governing body, members, or any class or group of members of a nonstock corporation . . . .").

[147] *Boilermakers Local 154 Ret. Fund*, 73 A.3d at 952.

[148] Jeff Montgomery, *Del. Federal Forum Ruling Could Open Door to Mischief*, LAW360 (Mar. 19, 2020, 11:38 PM), https://www.law360.com/securities/articles/1255189/del-federal-forum-ruling-could-open-door-to-mischief [https://perma.cc/JSX9-RMJA] (quoting Professor Lawrence A. Hamermesh); *see* Lipton, *supra* note 134.

[149] *See* Lipton, *supra* note 134; *cf.* Seafarers Pension Plan *ex rel.* Boeing Co. v. Bradway, No. 19 C 8095, 2020 WL 3246326, at *1 (N.D. Ill. June 8, 2020) (opining that *Salzberg*'s analysis is not controlling in cases concerning the enforceability of forum selection clauses regulating claims under the "1934 Act").

[150] *See generally, e.g.*, Ann Lipton, *The United States of Delaware*, BUS. L. PROF BLOG (Aug. 15, 2020), https://lawprofessors.typepad.com/business_law/2020/08/the-united-states-of-delaware.html [https://perma.cc/YN8W-4SAH] (discussing the conflicting Delaware and California law concerning shareholder inspection rights).

[151] IBS Fin. Corp. v. Seidman & Assocs., 136 F.3d 940, 949–50 (3d Cir. 1998).

accepted before *Salzberg*.[152] This approach has allowed for the law to grow against a predictable legal landscape.

CONCLUSION

Arbitration bylaws regulating federal securities claims are unenforceable. A corporation's internal affairs do not include securities claims because such claims do not turn on the rights between the corporation, directors, and current stockholders.

Considering the purpose of securities shareholder suits—mainly holding directors accountable—this is a just result. It would make little sense, given this national purpose, to shuttle federal securities claims off to arbitration forums. Such a scheme will lead to the deterioration of a developing national standard protecting against fraudulent securities conduct.

[152] Myron T. Steele, *Sarbanes-Oxley: The Delaware Perspective*, 52 N.Y.L. SCH. L. REV. 503, 506–07 (2008).