Sciabacucchi: Implications for D&O Liability and Insurance

May 5, 2020
The information and opinions expressed by our panelists today are their own, and do not necessarily represent the views of their employers or of PLUS.

The contents of these materials may not be relied upon as legal advice.
Questions

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Meet Your Presenters

Priya Cherian Huskins
Partner and SVP, Woodruff Sawyer

Brad Sorrels
Partner, Wilson Sonsini

Daniel J. Standish
Partner, Wiley
• The D&O litigation landscape: post-Cyan and Pre-Sciabacucchi

• Federal forum provisions: what are they, and how do they work?

• The Sciabacucchi case: background and route to the Delaware Supreme Court

• Insurance industry role in the case

• Key implications for defendants and their insurers
Shareholder Class Actions by Year of Filing

Securities Class Action Lawsuits

Number of Cases

<table>
<thead>
<tr>
<th>Year</th>
<th>Subprime/Credit</th>
<th>Classic</th>
<th>China HQ'd</th>
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<td>2010</td>
<td>106</td>
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<td>2011</td>
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<td>2012</td>
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<td>2016</td>
<td>196</td>
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<tr>
<td>2017</td>
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<tr>
<td>2018</td>
<td>223</td>
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<tr>
<td>2019</td>
<td>268</td>
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<tr>
<td>Q1 2020</td>
<td>54</td>
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<td>2.1%</td>
<td>2.9%</td>
<td>2.6%</td>
<td>2.8%</td>
<td>3.0%</td>
<td>3.5%</td>
<td>3.8%</td>
<td>4.3%</td>
<td>4.3%</td>
<td>5.0%</td>
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</table>

# of US Companies

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<td>5,017</td>
<td>4,900</td>
<td>4,943</td>
<td>4,909</td>
<td>5,139</td>
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<td>4,708</td>
<td>4,802</td>
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Note: Data current as of March 31, 2020. Historic public company data sourced from World Federation of Exchanges, NASDAQ and YCharts.

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Since the Supreme Court Decision on *Cyan* in March 2018, there has been a significant spike in Section 11 filings.

**Section 11 Cases and the Impact of *Cyan***

- **2017 (pre-Cyan):** 27 Cases
- **2018 (pre- & post-Cyan):** 42 Cases
- **2019 (post-Cyan):** 75 Cases

- **56% increase** 2017 > 2018
- **79% increase** 2018 > 2019

Source: Woodruff Sawyer DATABOX

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A troubling development: Parallel* Section 11 filings in federal and state courts has resulted in a 208% increase in filings from 2018 to 2019.

* A “parallel filing” is a case against the same company, its directors, and its officers on the same set of facts.

** Consisting of 19 companies that were sued in both state and federal courts, including one company sued in two separate state courts, and one company that was sued first in 2018 and had its parallel case filed in 2019.
Cases Settled – Non-IPO vs. IPO Cases

Non-IPO vs. IPO Cases*

<table>
<thead>
<tr>
<th>Category</th>
<th>Settled</th>
<th>Dismissed</th>
<th>Withdrawn</th>
</tr>
</thead>
<tbody>
<tr>
<td>Non-IPO - Federal Courts (1,218 Cases)</td>
<td>45%</td>
<td>10%</td>
<td>10%</td>
</tr>
<tr>
<td>IPO - Federal Courts (124 Cases)</td>
<td>25%</td>
<td>7%</td>
<td>16%</td>
</tr>
<tr>
<td>IPO - All State Courts (32 Cases)</td>
<td>75%</td>
<td>16%</td>
<td>9%</td>
</tr>
</tbody>
</table>

*Cases Settled from 2010 thru 1Q2020

Note: Eleven cases filed in CA state courts were voluntarily dismissed due to federal case settlements that included Section 11 allegations, and they are not included in the dismissal count for state court cases.

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D&O Insurance for IPO Companies

- **Increase in Pricing (averages)**
  - 2017 (Year): Less than $400K for the first $10M
  - 2019 (Q4): More than $2M for the first $10M

- **Increase in Self-Insured-Retentions**
  - 2017 (Year): $2M
  - 2019 (Q4): $10M
Federal forum provisions ("FFPs"): what are they and how do they work?
Federal Forum Provisions

• Federal Forum Provisions ("FFPs") are clauses in corporate organic documents designating federal courts as the exclusive forum for claims under the Securities Act of 1933 ("33 Act")
  – FFPs are similar to provisions designating Delaware courts as the exclusive forum for "internal corporate claims" – so-called Chevron bylaws – that were upheld in the Delaware Court of Chancery’s 2013 decision in Boilermakers Local 154 Ret. Fund v. Chevron Corp.
  – Later codified in 2015

• Professor Joe Grundfest of Stanford Law School initially proposed FFPs in 2016 in response to increasing numbers of ’33 Act lawsuits being brought in state courts.
Federal Forum Provisions

• An example of the text of a Federal Forum Provision:

  “Unless the Company consents in writing to the selection of an alternative forum, the federal district courts of the United States shall be the exclusive forum for the resolution of any complaint asserting a cause of action arising under the ’33 Act. Any person or entity purchasing or otherwise acquiring any interest in any security of the Company shall be deemed to have notice of and consented to this provision.”
The Sciabacucchi Litigation

- Blue Apron, Roku, and Stitch Fix each adopted largely identical FFPs in their pre-IPO charters; each company conducted an IPO in 2017

- The Court of Chancery Action
  - Matthew Sciabacucchi (pronounced “Sha-Ba-Cookie”), who held stock in each company, filed a complaint in the Delaware Court of Chancery in December 2017 seeking a declaration that the FFPs adopted by Blue Apron, Roku, and Stitch Fix were invalid under Delaware law
  - The parties filed cross-motions for summary judgement, and in a December 2018 opinion the court declared FFPs to be invalid
  - The court’s reasoning rested on its conclusion that “first principles” rendered FFPs invalid because the charters of Delaware corporations can only regulate “internal” claims, and for a variety of reasons (according to the court) FFPs are “external”
• Appeal to the Delaware Supreme Court
  
  – Blue Apron, Roku, and Stitch Fix appealed the decision to the Delaware Supreme Court and briefing (including briefs from 4 *amici*) was completed in fall 2019, with oral argument held in January 2020
  
  – The Supreme Court issued its unanimous (5-0) decision on March 18, 2020, reversing the lower court’s decision and declaring FFPs facially valid under Delaware law
  
  – The court concluded that regulation of "intra-corporate litigation" arising under federal or other positive law (i.e. ’33 Act claims) fits squarely within Section 102(b)(1) of the DGCL, and that the statute is not coterminous with the "internal affairs" doctrine or limited to regulating litigation arising under Delaware state law
Funding the Appeal

Insurance industry role in the case
Key Insurance Market Participants

8 D&O Insurance Carriers
- Allianz
- Allied World
- Beazley
- Chubb
- Great American
- Hiscox
- Old Republic
- Swiss Re

Two D&O Insurance Brokers
- Woodruff Sawyer
- Arthur J Gallagher
Key defense players

Professor Joe Grundfest
Stanford Law School

Wilson Sonsini Goodrich & Rosati

WilmerHale

Richards, Layton & Fingers
Implications of the Case for Policyholders and Insurers
Actions for Issuers: Adopt FFPs!

- Pre-IPO or Pre-Direct Listing Companies
- Companies that have recently gone public
  - Those with FFPs that were on hold
  - Those without
- Mature public companies
  - Planning to do a registered offering, including M&A?
  - ISS/Glass Lewis concerns
What lies ahead for issuers?

- Anticipated strategy by the plaintiffs’ bar?
- Next litigation battlefield: when and where?
- Strategic litigation considerations for issuers?
• Brokers – key datapoints to highlight in underwriting process
• Discounts versus premium pricing
• Insurers – considerations in the underwriting process based on the decision
Questions

Please submit using the question tool on user dashboard
Thank You!

Priya Cherian Huskins
Partner and SVP, Woodruff Sawyer

Brad Sorrels
Partner, Wilson Sonsini

Daniel J. Standish
Partner, Wiley
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Wednesday, May 13th
1:00pm - 2:00pm CT

http://plusweb.org/Events/Event-Info/sessionaltcd/WEBINAR0520
Thank you for your time.