

## California State Appellate Court: Upholds and Enforces a Federal Forum Provision Requiring Securities Act Claims to Be Brought in Federal Court (Securities Law Alert)

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On April 28, 2022, an intermediate California appellate court unanimously affirmed a lower court’s dismissal—based on a federal forum provision (“FFP”)—of a securities fraud class action against a Delaware corporation. [Wong v. Restoration Robotics, 2022 WL 1261423 \(Cal. App. Ct. 2022\) \(Miller, J.\)](#). Notably, this is the first appellate decision on the issue outside of Delaware since the Delaware Supreme Court’s decision upholding the facial validity of FFPs under Section 102(b)(1) of the Delaware General Corporation Law (“DGCL”) in [Salzberg v. Sciabacucchi, 227 A.D.3d 102 \(Del. 2020\)](#).

Soon after the defendant corporation’s IPO, the corporation experienced a stock drop and plaintiff sued in California state court alleging that defendant’s offering documents contained materially false and misleading statements in violation of Sections 11, 12(a)(2), and 15 of the Securities Act. Defendant moved to dismiss on the basis of its certificate of incorporation, which included an FFP stating that Securities Act claims must be brought in federal court unless the corporation consents in writing to an alternative forum. The trial court declined jurisdiction on the basis of the FFP and dismissed. On appeal, plaintiff primarily raised three arguments: (i) the FFP violated the Securities Act; (ii) the Delaware statutory scheme permitting the FFP violated the Commerce Clause and the Supremacy Clause; and (iii) the FFP was unenforceable as it was beyond investors’ reasonable expectations.

As to whether the FFP violated the Securities Act, the court rejected plaintiff’s argument that he had an unwaivable right to have his Securities Act claims heard in a state court under the anti-waiver provision of Section 77n.<sup>[1]</sup> The court reasoned that if the Exchange Act’s exclusive federal jurisdiction provision could be overridden by a forum selection agreement without violating that Act’s anti-waiver provision, then the Securities Act’s concurrent jurisdiction provision could likewise be overridden by a forum selection agreement without violating its anti-waiver provision. In support of this the court cited *Rodriguez de Quijas v. Shearson/American Express*, 490 U.S. 477 (1989), for the principle that the two statutes should be construed harmoniously because they are interrelated components of the federal regulatory scheme for securities transactions.

As to constitutionality, plaintiff argued that the corporation’s certificate of incorporation could not lawfully include an FFP as Delaware’s

statutory scheme violated the Commerce Clause and the Supremacy Clause. Noting that the presence of state action was required to bring a Commerce Clause claim, the court pointed out that generally a private entity, like the corporation, is not a state actor except in a few limited circumstances. The court observed that plaintiff’s challenge arose from the corporation’s decision as a Delaware corporation to include an FFP in its certificate of incorporation, which the court noted was permitted, but not required or even encouraged by Delaware law. The court held that it could not conclude that there was state action given plaintiff’s “failure to demonstrate any precedent for his Commerce Clause claim and given the reluctance of courts to expand the state action doctrine[.]” The court also “conclude[d] that Delaware has a legitimate interest in allowing its corporations to include FFPs in their certificates of incorporation, and that any burden on interstate commerce from the inclusion of an FFP does not exceed the benefits provided by the statute.”

Additionally, the court rejected plaintiff’s argument that Delaware’s statutory scheme permitting FFPs violated the Supremacy Clause, concluding that Section 115[2] of the DGCL “does not reflect any quarrel between Delaware and federal law over the content of the [Securities] Act or the extent of the remedies available under the [Securities] Act. Nor does it discriminate in favor of state law claims and against similar federal claims.”

As to the FFP’s enforceability, the court stated that under *Drulias v. 1st Century Bancshares*, 30 Cal.App.5th 696 (2018), a forum selection clause, like the FFP, “may be enforced unless there is a showing that it was outside the reasonable expectations of the weaker or adhering party or that enforcement would be unduly oppressive or unconscionable.” The court rejected plaintiff’s argument that an investor should not be expected to pore over a registration statement or otherwise investigate a company’s certificate of incorporation or expect to be bound by a novel provision. The court observed that forum selection clauses have long been in existence, and just because one is innovative does not mean that it is unenforceable. The court further refused to excuse investors from familiarizing themselves with a company’s disclosures, particularly in a corporation’s governing documents.

[1] Stating that “any condition, stipulation, or provision binding any person acquiring any security to waive compliance with any provision of this subchapter or of the rules and regulations of the Commission shall be void.”

[2] Section 115 provides that the certificate of incorporation or bylaws of a Delaware corporation may require that “internal corporate claims” be brought exclusively in Delaware state courts, and may not prohibit the bringing of such claims in Delaware state courts. “Internal corporate claims” as defined in Section 115, includes claims for which the Delaware corporate law confers jurisdiction upon the Court of Chancery.

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