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## What Happens in Delaware Need Not Stay in Delaware: How Trulia Can Strengthen Private Enforcement of the Federal Securities Laws

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## What Happens in Delaware Need Not Stay in Delaware: How *Trulia* Can Strengthen Private Enforcement of the Federal Securities Laws

*Class-action lawsuits have been used by private plaintiffs to enforce the federal securities laws since those laws were enacted in the 1930s. With the SEC retaining concurrent authority to enforce federal securities laws, a debate has emerged as to whether the private right of action helps or hinders public enforcement. The primary criticism of private securities litigation is that rent-seeking attorneys abuse the system by bringing frivolous litigation aimed at achieving a settlement and a fee. In the public merger context, the potentially disastrous consequences of failing to close an announced deal on time make corporations eager to settle potentially troublesome litigation. The government responded to the overabundance of securities lawsuits in the 1990s by tightening the reins on class-action securities litigation, making what was once low-hanging fruit for plaintiffs' attorneys more difficult to grasp. At the same time, there was a marked uptick in the number of class-action corporate lawsuits brought in state courts, in particular, in Delaware. These suits claim breach of fiduciary duty on the grounds that securities filings accompanying public merger announcements provided shareholders with insufficient or inadequate information.*

*This Comment claims that the wave of merger objection class-action suits arising in the mid-2000s should be properly viewed as federal securities law claims masquerading as corporate law claims, thus avoiding the heightened securities class-action requirements of the 1990s. In a recent case from the Delaware Court of Chancery, *In re Trulia, Inc. Shareholder Litigation*, Chancellor Bouchard established a new "plainly material" standard for approving class-action settlements where deficient federal securities filings are at issue. Because *Trulia* is properly viewed as a state court's response to deficient enforcement of the federal*

*securities laws, it has the potential to serve as a bellwether for the state of health of private enforcement of the federal securities laws.*

## CONTENTS

I. INTRODUCTION .....	716
II. AN OVERVIEW OF ENFORCEMENT OF THE FEDERAL SECURITIES LAWS .....	719
A. Public Enforcement and the Private Right of Action .....	719
B. The Case for Private Enforcement .....	722
III. THE PROBLEM OF OVERENFORCEMENT.....	724
A. Class-Action Lawsuits: From Federal Securities Law, to State Corporate Law .....	724
B. The Magnitude of Merger-Objection Litigation and the Disclosure-Only Settlement Epidemic.....	729
IV. <i>TRULIA</i> : THE DELAWARE COURT OF CHANCERY RESHAPES THE CLASS-ACTION SETTLEMENT APPROVAL LANDSCAPE .....	732
V. <i>TRULIA</i> 'S RELEVANCE TO THE FEDERAL SECURITIES LAWS.....	736
A. At Its Heart, <i>Trulia</i> Is a Federal Securities Law Decision .....	736
B. Exporting <i>Trulia</i> : A Precedent to Shore Up Private Enforcement in Securities Litigation.....	738
VI. CONCLUSION .....	741

## I. INTRODUCTION

There is a long-running debate in the context of the federal securities laws between the relative merits of public enforcement by the Securities and Exchange Commission (the “SEC”), and private enforcement, primarily in federal court, with claims brought by private plaintiffs.<sup>1</sup> Though advocates from both sides of the debate tout the benefits of one approach over the other, there is general agreement that private enforcement provides a necessary complement to the

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1. See generally Joseph A. Grundfest, *Disimplying Private Rights of Action Under the Federal Securities Laws: The Commission's Authority*, 107 HARV. L. REV. 961 (1994).

SEC's efforts.<sup>2</sup> However, the checkered history of private enforcement under the federal securities laws unavoidably elicits criticism that this system is compromised. Abusive overenforcement, caused by opportunistic plaintiffs' lawyers bringing meritless claims and seeking settlement and fee awards, have done serious damage to the reputation, and arguably even the ability, of private plaintiffs to efficiently enforce the federal securities laws through private causes of action in federal court.<sup>3</sup> Undoubtedly, private litigation plays an essential role, but excessive abusive litigation calls into question the efficacy of the private enforcement system.

What prior analyses discussing the effectiveness of private enforcement of the federal securities laws have failed to consider, and what this comment intends to add to this conversation, is that conditions on the ground have shifted dramatically since the mid-1990s and the face of securities class-action lawsuits has changed. Commentators remain focused on whether private enforcement is working in the context of securities litigation, without considering that, beginning in 1995, much of the abusive private litigation surrounding public company mergers traditionally brought as federal securities claims, has been brought instead as state corporate law claims, particularly in Delaware.<sup>4</sup>

Because of this shift in private securities law enforcement from the federal securities laws to state corporate law, assessing the health of private securities enforcement is incomplete without also considering the success of private enforcement in the areas of state corporate law that have swallowed much federal securities litigation. With this new perspective, a recent corporate law decision in the Delaware Court of

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2. See RICHARD A. POSNER, *ECONOMIC ANALYSIS OF LAW* 874 (9th ed. 2014) ("A mixed system . . . exploits complementarities between agencies and courts."); Howell E. Jackson & Mark J. Roe, *Public and Private Enforcement of Securities Laws: Resource-Based Evidence*, 93 J. FIN. ECON. 207, 237 (2009) ("The *relative value* of public and private enforcement is a key issue for understanding . . . financial markets . . . ." (emphasis added)).

3. Jackson & Roe, *supra* note 2, at 208.

4. See *infra* Section III.A.

Chancery, *In re Trulia, Inc. Stockholder Litigation*,<sup>5</sup> has altered the landscape of litigation involving public company mergers.

The *Trulia* holding applies a “plainly material”<sup>6</sup> standard when assessing the value of additional disclosures offered to shareholders to settle claims that prior merger-related disclosures were inadequate.<sup>7</sup> This is a significant blow to public merger litigation,<sup>8</sup> which, in a real sense, is the offspring of securities fraud class-action litigation.<sup>9</sup> Where a defendant could formerly settle such claims by providing an omitted piece of information, even if redundant or trivial, now, the Court of Chancery has said that it will not approve such settlements unless the additional information offered is actually of “plainly material” value to shareholders. This should ultimately serve to suppress the plaintiffs’ bar’s appetite for bringing strike suits (meritless class-action lawsuits that force settlement by threatening delays)<sup>10</sup> by reducing defendants’ ability to get to a quick settlement and fee award. With this new precedent established, the Court of Chancery has greatly reduced the availability of dry kindling fueling overenforcement in this area of the law. In this respect, Chancellor Bouchard has shown a willingness to take a stand against meritless securities litigation, where previously such efforts required multiple acts of Congress.<sup>11</sup> Consequently, jurisdictions outside of Delaware have already begun to adopt the Court of Chancery’s approach in public merger litigation.<sup>12</sup> Judges hearing class-action claims built around securities disclosures, whether arising as fiduciary duty claims under state corporate law or directly under the federal securities laws, should not shy away from applying *Trulia*. Doing so would reduce abusive litigation and breathe needed

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5. *In re Trulia, Inc. Stockholder Litig.*, 129 A.3d 884 (Del. Ch. 2016).

6. *Id.* at 898.

7. *Id.* at 907.

8. *Id.*

9. *See infra* Section III.A.

10. *See* Browning Jeffries, *The Plaintiffs’ Lawyer’s Transaction Tax: The New Cost of Doing Business in Public Company Deals*, 11 BERKELEY BUS. L.J. 55, 56 (2014) (stating that strike suits are the primary form of abuse in shareholder litigation).

11. *See infra* Section III.A.

12. *See In re Walgreen Co. Stockholder Litig.*, 832 F.3d 718 (7th Cir. 2016) (applying *Trulia* in approving disclosure-only settlement); *Raul v. Burke*, No. 15 CVS 16703, 2016 WL 382833, at \*1 n.2 (Super. Ct. N.C. Jan. 28, 2016) (applying the analysis Chancellor Bouchard developed in *Trulia*).

life back into the credibility of private enforcement of the federal securities laws.

## II. AN OVERVIEW OF ENFORCEMENT OF THE FEDERAL SECURITIES LAWS

### *A. Public Enforcement and the Private Right of Action*

Federal securities laws first came about in response to the stock market crash of 1929, which ushered in the Great Depression.<sup>13</sup> Congress responded with two key pieces of legislation: The Securities Act of 1933 (the “Securities Act”), and The Securities Exchange Act of 1934 (the “Exchange Act”).<sup>14</sup> In enacting these laws, Congress created a regime focused primarily on disclosure. Federal securities laws are built around detailed and extensive reporting requirements that aim to protect investors by requiring the full and accurate disclosure of all relevant information relating to securities offerings. In the case of public companies, this includes disclosing periodic financial statements, insider transactions, merger details, and so forth.<sup>15</sup> By committing to the federal securities laws questions of what must be disclosed, Congress left to the states the task of addressing the fairness of the underlying corporate actions and transactions driving the securities filings.<sup>16</sup> In practice, the SEC oversees the disclosure of corporate action, while states analyze corporate action through the framework of fiduciary duties found in corporate law.

Congress created the SEC with the mandate to administer the federal securities laws but did not give it an enforcement monopoly. Congress also created an explicit private right of action for many

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13. See Roberta S. Karmel, *Reconciling Federal and State Interests in Securities Regulation in the United States and Europe*, 28 BROOK. J. INT’L L. 495, 495 (2003); *What We Do*, U.S. SEC. & EXCHANGE COMMISSION, <https://www.sec.gov/about/whatwedo.shtml> (last modified June 10, 2013) (explaining that prior to the creation of the Securities Act and the Exchange Act, federal regulation of the securities market was effectively nonexistent, especially and perhaps most pointedly during the post-World War I boom in securities sales and offerings).

14. See THOMAS LEE HAZEN, *FEDERAL SECURITIES LAW 2–4* (Kris Markarian ed., 3d ed. 2011).

15. *Id.*

16. Karmel, *supra* note 13, at 498–99 (when dealing with public offerings, federal laws adopt “full disclosure philosophy,” while state law is merit based, focusing on whether capital structures are “fair, just and equitable”).

aspects of the federal securities laws, and for others, Congress implied a private right of action allowing private plaintiffs to police offenders through litigation.<sup>17</sup>

Those who criticize the federal courts' handling of private actions under federal securities law tend to focus on class-action lawsuits. They particularly criticize the notorious 10b-5 fraud suit, alleging that this judicially implied cause of action leads to frivolous suits and heightened agency costs. However, this focus is too narrow. Over the last decade, trends in private enforcement actions brought against public companies on securities-related grounds have morphed, at least on their face, from primarily federal securities law claims to state corporate law claims.

Under the federal securities laws, public corporations—those who have registered securities with the SEC—are subject to various filing requirements, disclosure requirements, and liability. Under state corporate law, state courts decide questions of fiduciary duty, including those related to securities disclosure. For this reason, many actions litigated against public corporations have both federal and state law implications.<sup>18</sup> A clear example of this emerges in the context of public mergers and acquisitions. Consider the following: a merger may include a tender offer.<sup>19</sup> If so, provisions of the tender offer are governed by the Exchange Act and must meet various reporting requirements administered by the SEC.<sup>20</sup> Questions over the merits of the merger, such as whether the consideration provided was fair or whether the transaction was in the best interest of the shareholders,

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17. *Id.*; Richard W. Painter, *Responding to a False Alarm: Federal Preemption of State Securities Fraud Causes of Action*, 84 CORNELL L. REV. 1, 2–3 (1998) (Securities Act created express remedies; Exchange Act implied remedies); *see also* Note, *Private Causes of Action for Option Investors Under SEC Rule 10b-5: A Policy, Doctrinal, and Economic Analysis*, 100 HARV. L. REV. 1959, 1961 (1987) (noting universal acceptance of an implied right of action under Rule 10b-5).

18. *See In re Oracle Corp. Derivative Litig.*, 824 A.2d 917, 924 (Del. Ch. 2003) (Strine, V.C.) (commenting that both an ongoing federal securities class-action lawsuit and a state corporate law derivative action for breach of fiduciary duty came from “substantively identical” facts).

19. A tender offer occurs when a potential buyer makes a public offer to acquire shares from each stockholder at a certain per share price.

20. *What Regulates M&A?*, section 1.1 to *Mergers & Acquisitions 2017*, INT’L COMP. LEGAL GUIDES (Feb. 28, 2017), <https://www.iclg.co.uk/practice-areas/mergers-and-acquisitions/mergers-and-acquisitions-2017/usa>.

fall under state corporate law.<sup>21</sup> Moreover, in an acquisition, the corporate law of the state of incorporation of the target company governs whether directors disclosed adequate information to enable shareholders to make an informed decision to vote in favor of a merger.<sup>22</sup> However, where votes for approval of a merger are solicited by proxy, federal law again steps in and the terms of the Exchange Act govern the proxy solicitation.<sup>23</sup> These examples illustrate that public corporate activity “falls within the dual jurisdiction of the federal government and the individual state in which the . . . company is incorporated.”<sup>24</sup>

The overlap between securities and corporate law has facilitated a relatively recent shift in private litigation surrounding public merger activity. Abusive class-action securities litigation brought by enterprising plaintiffs’ attorneys forced Congress to pass legislation making class-action securities litigation more difficult and costlier to bring, which makes meritless claims less appealing.<sup>25</sup> However, because the federal securities laws compel disclosure in advance of mergers by public companies in many instances, Congress’s efforts had an unintended effect. Securities disclosures provide information about recent merger activity that enables plaintiffs’ lawyers to quickly sue under state corporate law, claiming, among other things, that the directors breached their fiduciary duties by disclosing inadequate information. Because state corporate laws do not typically prohibit quick and easy class-action lawsuits, as do the federal securities laws, plaintiffs’ lawyers are able to bring class-action suits under state corporate law that are substantially like the claims brought as federal securities claims, namely faulty securities disclosures. To illustrate this point, consider a company that has entered into a merger agreement and must disclose this fact in its public filings with the SEC.<sup>26</sup> This revelation allows plaintiffs’ lawyers the chance to bring a lawsuit against the disclosing company relating to the quality of the

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21. See Karmel, *supra* note 13.

22. *What Regulates M&A*, *supra* note 20.

23. *Id.*

24. *Id.*

25. See Private Securities Litigation Reform Act of 1995 (PSLRA), Pub. L. No. 104-67, 109 Stat. 737 (codified as amended in scattered sections of 15 U.S.C.).

26. SECURITIES AND EXCHANGE COMMISSION, Form 8-K, Section 1, Item 1.01.



disclosures. The timing of the disclosure prescribed by the federal securities laws allows plaintiffs to sue the company before the merger closes. This gives the plaintiffs' lawyers considerable leverage in negotiating a settlement with the defendant who is eager to avoid delay in the now public merger process.<sup>27</sup> Because legislation in the 1990s rendered federal securities class-action lawsuits more cumbersome, plaintiffs' lawyers shifted their preferred causes of action from those of faulty disclosures under the Securities Act and fraud under the Exchange Act to breaches of fiduciary duty under state corporate law. The new approach simply uses the same information in the same securities filings previously used to bring claims under federal securities laws to bring nearly identical claims under state corporate law. In hindsight, this seems like a natural shift. These claims are, at their heart, still securities claims (they originate from, and are often focused primarily on, federal securities disclosures). For this reason, judicial action at the state level to curb these claims is pertinent to, and indicative of, the health and efficiency of private enforcement of the federal securities laws.

### *B. The Case for Private Enforcement*

Proponents of private enforcement of the federal securities laws tout the instrumental role that it plays in deterring fraudulent corporate behavior.<sup>28</sup> The general premise is that as private enforcers bring claims against corporate defendants, the likelihood of punishment increases, and this has a deterrent effect on bad behavior.<sup>29</sup> Some argue that legislative restrictions to the private right of action in securities laws are the culprit for the accounting scandals of the early 2000s and the economic collapse of 2008.<sup>30</sup> Private parties should be unfettered in their ability to help deter federal securities violations

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27. Jill E. Fisch, *Class Action Reform: Lessons from Securities Litigation*, 39 ARIZ. L. REV. 533, 535 (1997) (observing that corporate defendants often settle meritless claims because of the "enormous financial burden of litigation").

28. Steven A. Ramirez, *The Virtues of Private Securities Litigation: An Historic and Macroeconomic Perspective*, 45 LOY. U. CHI. L.J. 669, 671 (2014).

29. Keith L. Johnson, *Deterrence of Corporate Fraud Through Securities Litigation: The Role of Institutional Investors*, 60 L. & CONTEMP. PROBS. 155, 162 (1997).

30. Ramirez, *supra* note 28, at 671–73.

through private action and market forces will limit abusive litigation.<sup>31</sup> While this argument represents a polar extreme of the conversation, it relies in large part on the well-accepted premise that private enforcement is a necessary, well-equipped mechanism for enforcing the laws built to keep investors safe.<sup>32</sup>

It is widely recognized that the SEC is not equipped to carry out its mandate without essential help from private enforcers.<sup>33</sup> One reason for this is that the SEC does not have the resources to enforce the federal securities laws without additional help.<sup>34</sup> Another is that the SEC's incentives do not always align with those of private enforcers and investors,<sup>35</sup> and private enforcement is necessary to protect the latter group's interests. Yet another is that the SEC is hampered from its mission by political and partisan pressures in a way that private parties are not.<sup>36</sup> However, the system of private enforcement that has grown up with the securities laws has proven susceptible to abuse. The new standard introduced in *Trulia* has the potential to suppress a sizeable source of this abuse and breath added credibility into private litigation as an effective enforcement mechanism.

One prevalent criticism of private enforcement in the securities law context is that abusive litigation grew so problematic that Congress had to enact the Private Securities Litigation Reform Act (PSLRA) to

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31. *See id.*

32. *See* J.I. Case Co. v. Borak, 377 U.S. 426, 432 (1964).

33. *See id.*; S. REP. NO. 104-98, at 37-38 (1995) (Senators Sarbanes, Bryan, and Boxer repeatedly acknowledging importance of private enforcement mechanism); Brief of AARP & North American Securities Administrators Ass'n, Inc. as Amici Curiae in Support of Respondents at 6, Janus Capital Grp. v. First Derivative Traders, 564 U.S. 135 (2011) (No. 09-525) (citing William R. McLucas, former director of the Enforcement Division of the SEC, who said the private right of action under Rule 10b-5 is a necessary supplement).

34. Brief of AARP & North American Securities Administrators Ass'n, Inc. as Amici Curiae in Support of Respondents, *supra* note 33, at 6.

35. *Id.* at 12; *see also* Michael Lewis & David Einhorn, *The End of the Financial World as We Know It*, N.Y. TIMES (Jan. 3, 2009), <http://www.nytimes.com/2009/01/04/opinion/04lewisinhorn.html>.

36. Mark Schoeff Jr., *How Partisan Politics Have Poisoned the SEC*, INVESTMENTNEWS (May 10, 2015, 12:01 am), <http://www.investmentnews.com/article/20150510/REG/150509926/how-partisan-politics-have-poisoned-the-sec> (quoting New Jersey Representative and House Financial Services Committee member Scott Garrett as saying "[u]nfortunately, it appears that the SEC is becoming more political and more distracted from its core mission than ever").

reign it in.<sup>37</sup> This Comment argues that Chancellor Bouchard's recent refusal to approve disclosure-only settlements in *Trulia, Inc. Stockholder Litigation*<sup>38</sup> has the potential to make significant progress in stemming the tide of abusive private enforcement of state corporate law claims against public companies that are, at heart, federal securities claims. In that sense, Chancellor Bouchard's insistence on a higher standard and rejection of disclosure-only settlements can be seen as a continuation of Congress's intention behind the PSLRA. Because of the clear nexus between the *Trulia* decision and federal securities laws, state and federal judges hearing disclosure-focused corporate claims and federal securities claims should be willing to look to *Trulia* for guidance. In so doing, *Trulia* can help repair the reputation of private enforcement of the federal securities laws damaged by decades of abuse.

### III. THE PROBLEM OF OVERENFORCEMENT

#### A. Class-Action Lawsuits: From Federal Securities Law, to State Corporate Law

Since the mid-1990s, Congress has been pushing to quell a growing tide of securities class-action litigation, yet the unintended effect has been to push litigants<sup>39</sup> from federal securities law claims to state corporate law merger objection claims.<sup>40</sup> As fraud-on-the-market litigation under Rule 10b-5 grew particularly troublesome and expansive,<sup>41</sup> Congress stepped in with a legislative fix. The solution

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37. Michael B. Dunn, Note, *Pleading Scierter After the Private Securities Litigation Reform Act: Or, a Textualist Revenge*, 84 CORNELL L. REV. 193, 194–95 (1998).

38. *In re Trulia, Inc. Stockholder Litig.*, 129 A.3d 884, 907 (Del. Ch. 2016).

39. While litigation of this type has indeed shifted to state courts under corporate law causes of action, this does not necessarily reflect a shift in preference on behalf of litigants. This migration is most likely a calculated strategy of the plaintiff's bar, not its clients. In fact, Congress described the PSLRA as an "attack on lawyer-driven litigation," which Newt Gingrich characterized as "inherently abusive." Fisch, *supra* note 27, at 533–35.

40. *See supra* Section II.A.

41. *See Blue Chip Stamps v. Manor Drug Stores*, 421 U.S. 723, 739 (1975). One commentator described this process as follows:

Some lawyers went further in an effort to generate legal fees by developing securities fraud litigation. Witnesses before Congress testified to lawyers maintaining stables of named plaintiffs who were available for use as class representatives . . . . These plaintiffs received bonus payments for their participation but had little actual role in

was twofold: raise the bar for prevailing on securities class-action claims in federal court,<sup>42</sup> and funnel more securities litigation away from state courts into the federal system.<sup>43</sup> In 1995, Congress passed the Private Securities Litigation Reform Act (PSLRA)<sup>44</sup> in response to “perceived abuses of the class-action vehicle in litigation involving nationally traded securities.”<sup>45</sup> The PSLRA applied to all class-action securities cases brought in federal court<sup>46</sup> and operated by implementing “procedural protections”<sup>47</sup> that made it more difficult to prevail on those claims.<sup>48</sup> Congress’s stated intent in enacting the PSLRA was to prevent private securities litigation from being “undermined by those who seek to line their own pockets by bringing abusive and meritless suits.”<sup>49</sup> The market reacted by electing to bring these securities claims in state court instead,<sup>50</sup> so Congress followed up the PSLRA with the Securities Litigation Uniform Standards Act of 1998 (SLUSA).<sup>51</sup> SLUSA ensured that securities class-action suits could no longer be brought under state securities laws, only federal law,<sup>52</sup> and that federal securities class-action suits in state court could be removed to federal court.<sup>53</sup> In 2005, Congress followed up the SLUSA with the Class Action Fairness Act (CAFA).<sup>54</sup> Unlike the

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the subsequent cases and were often ignorant of the nature of the claims to which they lent their names.

Fisch, *supra* note 27, at 536.

42. See 15 U.S.C. § 78u-4 (2012); HAZEN, *supra* note 14, at 62.

43. See generally Painter, *supra* note 17.

44. Private Securities Litigation Reform Act of 1995 (PSLRA), Pub. L. No. 104-67, 109 Stat. 737 (codified as amended in scattered sections of 15 U.S.C.).

45. Merrill Lynch, Pierce, Fenner & Smith Inc. v. Dabit, 547 U.S. 71, 81 (2006).

46. 15 U.S.C. § 77z-1(a)(1) (2012).

47. Jay B. Kasner et al., Merrill Lynch v. Dabit: *The Supreme Court Forecloses State Law “Holders” Claims*, INSIGHTS, May 2006, at 1, 1 (quoting H.R. REP. NO. 104-369, at 32 (1995) (Conf. Rep.)).

48. See Marvin L. Frank, *Staying Derivative Actions Pursuant to PSLRA and SLUSA*, N.Y.L.J. (Oct. 21, 2005), <https://www.law.com/newyorklawjournal/almID/900005439409>.

49. H.R. REP. NO. 104-369, at 31 (1995) (Conf. Rep.).

50. Kasner et al., *supra* note 47, at 2.

51. Securities Litigation Uniform Standards Act of 1998 (SLUSA), Pub. L. No. 105-353, 112 Stat. 3227 (codified as amended in scattered sections of 15 U.S.C.).

52. See Merrill, Lynch, Pierce, Fenner & Smith Inc. v. Dabit, 547 U.S. 71, 74 (2006).

53. Leo E. Strine, Jr. et al., *Putting Stockholders First, Not the First-Filed Complaint*, 69 BUS. LAW. 1, 9-10 (2013).

54. See Class Action Fairness Act of 2005 (CAFA), Pub. L. No. 109-2, 119 Stat. 4 (codified as amended in scattered sections of 28 U.S.C.).

PSLRA and the SLUSA which applied only to securities class-action suits, CAFA applied to all class-action suits, allowing defendants to remove the claims from state court (which lawmakers felt were too plaintiff friendly)<sup>55</sup> to federal court.<sup>56</sup>

Congress's intention with these three pieces of legislation was to concentrate securities class-action suits in the federal courts, where expertise in handling these matters could develop and abusive litigation could be reined in.<sup>57</sup> If the measure of success for Congress's efforts is the overall reduction of abusive securities litigation, then, objectively, Congress had some initial success.<sup>58</sup> However, viewed through a broader lens, the legislation had an unintended, unforeseen, and somewhat opposite effect: plaintiffs' lawyers were turned off by the increased resources required to successfully bring class-action securities claims in federal court and balked at the prospect of securities litigation in state court being removed to federal court.<sup>59</sup> Litigants instead began pursuing claims under state corporate law.

While the CAFA generally allows all class-action litigation to be removed to federal court, it contains two exemptions that contributed to the preference for state corporate law claims. The first exemption,

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55. S. REP. NO. 109-14, at 4 (2005) (“[S]tate court[] . . . judges have reputations for readily certifying classes and approving settlements without regard to class member interests.”).

56. 28 U.S.C. § 1453(b) (2012) (“In General - A class action may be removed to a district court of the United States . . .”).

57. See Jill E. Fisch et al., *Confronting the Peppercorn Settlement in Merger Litigation: An Empirical Analysis and a Proposal for Reform*, 93 TEX. L. REV. 557, 602 (2015) (arguing that merger disclosure claims be relegated away from state courts to federal courts, which are more specialized in applying the securities laws, and be maintained as claims under federal securities laws, which are more highly developed than state corporate law); Jeffries, *supra* note 10, at 65–66 (stating that the PSLRA and the SLUSA were tailored for the peculiarities of the securities litigation market and were designed to channel more litigation to federal fora); see also Kasner et al., *supra* note 47, at 2 (noting the specialized nature of the PSLRA and SLUSA in combatting abuse of securities litigation).

58. See Stephen Choi et al., *The Screening Effect of the Private Securities Litigation Reform Act 6–7* (Univ. of Mich. Law Sch., Law & Econ. Working Papers Archive: 2003-2009, Art. 69, 2007) (noting that securities litigation dipped after the PSLRA passed, but levels have since recovered, though dismissal is now more likely); Amanda M. Rose, *Better Bounty Hunting: How the SEC's New Whistleblower Program Changes the Securities Fraud Class Action Debate*, 108 NW. U. L. REV. 1235, 1236 (2014) (PSLRA dealt a “major blow” to fraud-on-the-market securities class actions). *But see* SVETLANA STARYKH & STEFAN BOETTRICH, NERA ECON. CONSULTING, RECENT TRENDS IN SECURITIES CLASS ACTION LITIGATION: 2015 FULL-YEAR REVIEW 2 (2016) (confirming rising trend in post-PSLRA securities litigation).

59. Strine et al., *supra* note 53, at 9–10.

found in sections 1453(d)(1) and (3), provides relief from the removal provision for claims concerning securities.<sup>60</sup> On its face, this exemption appears to preserve a securities class-action plaintiff's ability to maintain its claim in state court. In application, however, the confusing intersection of the CAFA's removal-enabling provisions, this carveout for securities claims, an explicit non-removal provision in the Securities Act, and the pro-federal jurisdiction provisions of the PSLRA and the SLUSA cast some doubt on whether securities class actions could be removed under CAFA.<sup>61</sup> As courts took up the issue, no clear consensus emerged, leaving plaintiffs uncertain of what to expect if they initiated securities class action in state court.<sup>62</sup> In contrast, the other class-action removal exemption in the CAFA was unambiguous. Section 1453(d)(2) exempted claims dealing with "internal affairs or governance . . . aris[ing] under or by virtue of the laws of the State in which [a] corporation or business enterprise is incorporated or organized."<sup>63</sup> This language leaves little doubt that class-action corporate law claims are not removable to federal court under CAFA. This presented class-action plaintiffs hoping to avoid federal court with a choice: bring a securities claim and face the possibility of removal to federal court under CAFA, or bring a state corporate law claim and enjoy relative certainty of non-removal. For many litigants, the choice for corporate law claims was clear.

The reaction of the plaintiffs' bar to Congress's legislative attempts throughout the 1990s and 2000s to federalize securities class-action lawsuits throws an important point into sharp relief: almost any given corporate action by a public company that might injure shareholders' rights can potentially be addressed under either the federal securities laws or state corporate law. High-dollar transactions by public companies are often targeted up front because

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60. 28 U.S.C. § 1453(d)(1), (3) (2012).

61. See MAYER BROWN, EMERGING ISSUES IN SECURITIES LITIGATION: THE SEVENTH CIRCUIT'S RECENT INTERPRETATIONS OF CAFA AND SLUSA FAVOR DEFENDANTS IN PURPORTED SECURITIES CLASS ACTIONS (2009), <https://www.mayerbrown.com/publications/Emerging-Issues-in-Securities-Litigation-The-Seventh-Circuits-recent-interpretations-of-CAFA-and-SLUSA-favor-defendants-in-purported-securities-class-actions-03-26-2009/> (describing a circuit split with courts grappling with the interplay of these various statutes, and no consistent interpretation emerging).

62. See *id.*

63. 28 U.S.C. § 1453(d)(2) (2012).

public disclosures provide detailed fodder that plaintiffs' lawyers can act on quickly.<sup>64</sup> Additionally, the corporate resources invested in the transaction make settlement a no-brainer for corporate managers eager to close their deal.<sup>65</sup> In fact, from 2009 to 2014, the percentage of mergers valued over \$100,000,000 that faced shareholder litigation exceeded 90%.<sup>66</sup> In 2014, 75% of these lawsuits settled before the merger was consummated.<sup>67</sup> It is clear from these figures that plaintiffs lawyers capitalize on the ease of bringing merger litigation and the willingness of defendants to settle.

The contemporaneous shift away from federal securities class-action lawsuits prompted by the PSLRA, SLUSA and CAFA, along with the entrance onto the scene and subsequent blossoming of merger litigation under state corporate law,<sup>68</sup> should not be ignored or dismissed as coincidental. Merger objection litigation is, in this sense, a new face of the "abusive and meritless" securities litigation that Congress sought to quell by enacting the PSLRA.<sup>69</sup> Actions in state courts to combat this problematic litigation are directly applicable in the context of the federal securities laws.

The migration of the plaintiffs' bar from actions under the federal securities laws to actions under state corporate law has raised the ire of many state court judges.<sup>70</sup> In January 2016, Chancellor Bouchard of the Delaware Court of Chancery handed down a ruling in *Trulia* that represents a major milestone in the attempt to curtail merger

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64. K. Tyler O'Connell et al., *Reducing the "Deal Tax": Delaware's Recent Scrutiny of Nonmonetary Settlements*, BUS. L. TODAY, Oct. 2015, at 1, 1, <https://www.americanbar.org/content/dam/aba/publications/blt/2015/10/deal-tax-201510.authcheckdam.pdf>.

65. Fisch, *supra* note 27, at 535–36 (noting that corporate defendants face "pressure . . . to settle even weak cases" stemming from the cost of defense and other institutional and deal-based structures).

66. CORNERSTONE RESEARCH, SHAREHOLDER LITIGATION INVOLVING ACQUISITIONS OF PUBLIC COMPANIES: REVIEW OF 2015 AND 1H 2016 M&A LITIGATION 1 (2016) [hereinafter CORNERSTONE 2016].

67. *Id.*

68. RENZO COMOLLI ET AL., NERA ECON. CONSULTING, RECENT TRENDS IN SECURITIES CLASS ACTION LITIGATION: 2012 FULL-YEAR REVIEW 5 fig.3 (2013) (showing that merger objection litigation took off beginning in 2006).

69. H.R. REP. NO. 104-369, at 31 (1995) (Conf. Rep.).

70. See *In re Trulia, Inc. Stockholder Litig.*, 129 A.3d 884, 898 (Del. Ch. 2016) (Bouchard, C.) (describing merger litigation that seeks additional disclosure and a settlement as the "historically trodden but suboptimal path").

objection litigation abuse.<sup>71</sup> This case should be viewed as a continuation of Congress's effort to remedy private litigation's susceptibility to overenforcement in the securities context.<sup>72</sup> Moreover, it demonstrates a judicial willingness to stand up to frivolous securities-based litigation, a willingness which Congress found lacking in the lead up to the PSLRA.<sup>73</sup> The *Trulia* decision has implications beyond state corporate law, and it should be considered and applied by state court judges outside of Delaware, as well as federal court judges when hearing litigation arising under, or implicating, the federal securities laws.

*B. The Magnitude of Merger-Objection Litigation and the Disclosure-Only Settlement Epidemic*

Abusive class-action lawsuits are commonly referred to as “strike suits.”<sup>74</sup> A strike suit, in the generic corporate sense, is a shareholder claim challenging certain elements of a securities filing or corporate action, whether proposed or consummated. The plaintiff knows that corporate mechanics will incentivize defendants to settle quickly, even if the claim has no underlying merit, in order to facilitate a securities offering, merger, large transaction, other deal timeline, or simply to avoid costly and potentially messy litigation.<sup>75</sup> While strike suits crop up in all corners of corporate and securities laws, there is a particular form of strike suit unique to securities and public merger claims

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71. *Id.*

72. See generally Jeffries, *supra* note 10, at 56 (noting that a response from both the federal legislature and state courts is the natural result of unbearably high agency costs in corporate litigation).

73. H.R. REP. NO. 104-369, at 31 (House and Senate Committees heard evidence of a variety of abusive practices committed in private securities litigation. The report notes that “[t]hese serious injuries to innocent parties are compounded by the reluctance of many judges to impose sanctions under Federal Rule of Civil Procedure 11, except in those cases involving truly outrageous misconduct.”).

74. See, e.g., Broc Romanek, *Disclosure-Only Settlements: In re Trulia As Death Knell?*, DEAL LAWYERS (Jan. 25, 2016), <https://www.deallawyers.com/blog/2016/01/disclosure-only-settlements-in-re-trulia-as-death-knell.html> (labeling *Trulia* the latest in a long line of strike suits).

75. See Gregory A. Markel & Gillian Groarke Burns, *Expert Q&A on Judicial Activism and Disclosure-Only Settlements in Delaware*, PRAC. L.J., Aug.–Sept. 2006, at 22, 22–23.



known as a “disclosure-only settlement.”<sup>76</sup> These suits challenge certain board actions relating to, and substantive elements of, a proposed merger. When the parties move to settle, the settlement proposal offers shareholders only additional disclosures and, of course, attorney’s fees for the plaintiffs’ lawyers.<sup>77</sup>

Disclosure-only settlements are enabled because corporate and securities law provisions require certain disclosures for significant corporate transactions and securities offerings. Disclosure-only settlements are widespread.<sup>78</sup> They occupy an area of law that implicates both state corporate and the federal securities laws,<sup>79</sup> and they rose to prominence just as federal legislation made securities fraud class actions more difficult to bring. This nexus to the federal securities laws means that how judges deal with disclosure-only settlements is a strong proxy for the health of private enforcement of claims sounding in the federal securities laws. To the extent that state and federal courts apply *Trulia*’s “plainly material” standard, the potential for abusive securities-related litigation will diminish.

Over the course of the last decade,<sup>80</sup> disclosure-only settlements have become a familiar and burdensome presence in merger litigation, both within Delaware and without.<sup>81</sup> The plaintiffs’ bar grew so aggressive that litigation was filed in nearly 90% of all announced mergers prior to 2016.<sup>82</sup> Plaintiffs’ firms often bring suit days, and sometimes mere hours, after a proposed merger proposal is announced

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76. See Peter J. Walsh, Jr. & Aaron R. Sims, *Trulia and the Demise of “Disclosure Only” Settlements in Delaware*, BUS. L. TODAY, Feb. 2016, at 1, 1, <https://www.americanbar.org/content/dam/aba/publications/blt/2016/02/delaware-insider-201602.authcheckdam.pdf>.

77. See *In re Sauer-Danfoss Inc. S’holders Litig.*, 65 A.3d 1116 *passim* (Del. Ch. 2011) (Laster, V.C.) (characterizing the proposed settlement in *Sauer-Danfoss* as a “disclosure-only” settlement, and spending the entire opinion discussing the attributes of this type of settlement).

78. See *supra* Part III.

79. See *supra* Section II.A.

80. See *supra* Part III (noting that the burgeoning of merger objection litigation began in 2006 on the heels of the PSLRA, SLUSA, and CAFA).

81. *In re Trulia, Inc. Stockholder Litig.*, 129 A.3d 884, 898 (Del. Ch. 2016) (holding that the disclosure-only settlement is the “historically trodden but suboptimal path”); William Foley et al., *In re Riverbed: The Beginning of the End for Disclosure-Only Settlements in M&A Cases?*, ORRICK (Sept. 29, 2015), <http://blogs.orrick.com/securities-litigation/2015/09/29/in-re-riverbed-the-beginning-of-the-end-for-disclosure-only-settlements-in-ma-cases/>.

82. CORNERSTONE 2016, *supra* note 66 (noting that merger litigation for announced deals over \$100 million in value has dropped below 90% for first time since 2009, possibly because of the *Trulia* ruling); see also *In re Sauer-Danfoss*, 65 A.3d at 1119.

to the public.<sup>83</sup> The speed with which claims are filed allows plaintiff's lawyers virtually no time for thorough analysis of the merits of the transaction.<sup>84</sup> Chancellor Bouchard has noted that it is highly unlikely, if not impossible, that nearly every proposed merger involves a breach of fiduciary duty, as plaintiffs claim.<sup>85</sup> Instead, there is wide consensus that the claims are usually frivolous, and because corporate defendants settle in the vast majority of cases, these suits likely serve to support a cottage industry of "rentseeking" attorneys.<sup>86</sup> The practice has grown so embedded and predictable that corporate managers, when structuring a merger, factor in a "deal-tax" to cover settlement and attorney's fees that will need to be paid to settle the inevitable shareholder claims.<sup>87</sup> This type of litigation, long familiar under federal

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83. See *In re Sauer-Danfoss*, 65 A.3d at 1119 (lawsuit filed "hours after" announced tender offer plan); Dwight W. Stone II et al., *Dealing with the Inevitable: Practical Considerations in Defending Merger Objection Lawsuits*, FOR DEFENSE, Oct. 2013, at 56, [http://www.wtplaw.com/sites/default/files/document\\_pdf/DRI%20-%20Dealing%20with%20the%20Inevitable%20-%20October%202013.pdf](http://www.wtplaw.com/sites/default/files/document_pdf/DRI%20-%20Dealing%20with%20the%20Inevitable%20-%20October%202013.pdf) (class-action law firm press releases announcing litigation often follow within hours of merger announcements); see also *In re Philip Morris Sec. Litig.*, 872 F. Supp. 97, 98–99 (S.D.N.Y. 1995) (shareholders filed suit five hours after announcement that Phillip Morris would lower cigarette prices), *aff'd in part sub nom.*, *San Leandro Emergency Med. Grp. Profit Sharing Plan v. Philip Morris Co.*, 75 F.3d 801 (2d Cir. 1996).

84. *Trulia*, 129 A.3d at 892 (noting lawyer's complaints are "hastily drafted").

85. Transcript of Settlement Hearing and Rulings of the Court at 38, *Assad v. World Energy Sols., Inc.*, C.A. No. 10324-CB (Del. Ch. Aug. 20, 2015) (statement of C. Bouchard) ("It just can't be that there are meaningful disclosure violations in every single M&A case that's being filed in this court. And I think there's a lot of concern that a lot of the stuff that has been occurring historically is very fluffy.").

86. See CORNERSTONE 2016, *supra* note 66, at 4 (noting that by 2014, nearly 80% of merger litigation settled before deal closing, but that since then, that rate has dropped to 56%, potentially as a result of *Trulia*); Jackson & Roe, *supra* note 2, at 208; Markel & Burns, *supra* note 75, at 2–3.

87. O'Connell et al., *supra* note 64; see also Britt K. Latham & James P. Smith III, *The Future of Disclosure-Only Settlements*, N.Y.L.J. (May 23, 2016), <https://www.law.com/newyorklawjournal/almID/1202758057785/the-future-of-disclosureonly-settlements> (acknowledging the prevalence of the term "deal tax," suggesting also a more charitable label: "deal insurance").

securities law, has become increasingly prevalent under state corporate law.

#### IV. *TRULIA*: THE DELAWARE COURT OF CHANCERY RESHAPES THE CLASS-ACTION SETTLEMENT APPROVAL LANDSCAPE

For years, judges in Delaware acknowledged the merger litigation problem but routinely approved disclosure-only settlements, often begrudgingly.<sup>88</sup> In recent cases to come before the Court of Chancery, the judges indicated that their patience was running thin and that a solution to end abusive disclosure-only settlements was needed.<sup>89</sup> The solution finally came in *Trulia* when Chancellor Bouchard refused to approve the settlement proposed by the parties, adopting a new “plainly material” standard, and ushering a new paradigm into the merger objection litigation regime. This new standard ought to be incorporated into all jurisprudence dealing with issues rooted in the federal securities laws.

The facts of *Trulia* were, by 2016 when the case found its way to the Court of Chancery, fairly garden variety. This is only to say that *Trulia* was not a response to a novel or unique problem. Instead, it was the straw that broke the Court of Chancery’s back. The facts being more or less generic, a cursory treatment should suffice to convey the importance of the court’s ruling.

In brief, in 2015, two real estate data firms, Trulia, Inc., and Zillow, Inc., agreed to an all-stock merger wherein Zillow would acquire Trulia.<sup>90</sup> As is required by the Delaware General Corporate Law (DGCL),<sup>91</sup> and typical under the corporate law of most U.S. jurisdictions,<sup>92</sup> this type of merger must be approved by shareholder vote. In anticipation of a proxy vote to approve the deal, the merger

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88. *In re Sauer-Danfoss*, 65 A.3d at 1141 (approving a fee award, but a significantly reduced one, noting that the “case [did] not merit a significant award”); *Trulia*, 129 A.3d at 894 (noting the Court’s criticism of fee requests from settlements based on disclosures of “marginal value”).

89. *See Trulia*, 129 A.3d at 892.

90. *Id.* at 886.

91. DEL. CODE ANN. tit. 8, § 251(b)–(c) (2016).

92. *See* Julian Velasco, *The Fundamental Rights of the Shareholder*, 40 U.C. DAVIS L. REV. 407, 418–19 (2006) (speaking of shareholder rights generally, Velasco categorizes the right to approve a merger as “fundamental” in many jurisdictions); MODEL BUS. CORP. ACT § 11.04(b) (2016).

was publicly announced,<sup>93</sup> and accompanying public disclosures were made with the SEC as required of public companies under the federal securities laws.<sup>94</sup> Almost immediately, four shareholders separately instigated class-action lawsuits against Trulia's directors, claiming that certain aspects of the merger were unfair and that the board's approval was a breach of fiduciary duty.<sup>95</sup> Trulia quickly moved to settle the claims. The Court of Chancery responded by issuing a decision addressing the parties' request for approval of the terms of their proposed settlement.<sup>96</sup>

The shareholders in *Trulia* brought a variety of claims against the directors. After the four outstanding class-action suits were consolidated, four claims leveled at the Trulia board remained: (1) that the board did not get the best price possible; (2) that the company was improperly valued; (3) that agreeing to a no-shop provision was detrimental to the company; and (4) that the board "disseminat[ed] materially false and misleading disclosures to the Company's stockholders."<sup>97</sup> Of these claims, the fourth was clearly the most important to the plaintiffs because it was the only claim supported in the plaintiffs' briefing or discussed in any detail in Chancellor Bouchard's opinion.<sup>98</sup> It is also important to note that the first three claims (which were largely ignored) were questions of pure corporate law, while the fourth claim (on which the entire decision rested) was a question of pure federal securities law.

Shortly after the claims were filed, Trulia produced a memorandum of understanding agreeing to settle the claims by providing additional disclosures to its shareholders.<sup>99</sup> In time, the company provided additional information in its proxy materials and in accordance with securities laws about, among other things, the role

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93. *Trulia*, 129 A.3d at 886; see also Monique D. Hayes, *When the Tides Turn: Fiduciary Duties of Directors and Officers of Distressed Companies*, BUS. L. TODAY, July 2015, at 1 (explaining the duty of loyalty and care owed to shareholders of a publicly traded company).

94. 17 C.F.R. § 230.165(a) (2017).

95. *Trulia*, 129 A.3d at 886–87.

96. *Id.* at 887.

97. *Id.* at 889. But see Stipulation and Agreement of Compromise, Settlement, and Release at 2–3, *In re Trulia*, 129 A.3d 884 (No. 10020-CB) (listing five original class-action suits).

98. *Trulia*, 129 A.3d at 889.

99. *Id.*

that certain analysts played in the transaction process and the methodology that investment banks used in valuing the acquisition.<sup>100</sup> In exchange for these disclosures and a commitment from Trulia not to oppose a request for \$375,000 in attorney's fees, the plaintiffs agreed to the settlement and to release Trulia from all present and future claims.<sup>101</sup>

Typically, a settlement between a plaintiff and a defendant ends litigation. The defendant offers payment to the plaintiff, who releases the defendant from liability regarding the underlying claims. Individual plaintiffs are usually free to broker any settlement they wish—courts do not typically intervene. However, in the class-action context, a settlement affects more than just the named plaintiffs because all members of the class are bound by the judgment.<sup>102</sup> If individuals not immediately party to litigation will be bound and precluded in the future from bringing further claims, then it is important to safeguard against plaintiffs accepting settlements that may be adverse to other class members' interests or rights.<sup>103</sup> For this reason, a class-action settlement must be proposed to the court, and the judge must review the settlement to see that it is "fair, reasonable, and adequate," and either approve or reject it.<sup>104</sup>

In *Trulia*, Chancellor Bouchard reviewed the proposed settlement, found that it did not adequately protect the interests of the class members, and rejected it.<sup>105</sup> The plaintiff's attorneys sought to justify the settlement on the premise that the three major stakeholders would be left in the following favorable positions: the shareholders would receive valuable additional disclosures, the corporation would receive the assurance that the deal would not be challenged further, and the plaintiffs' attorneys would take home a fee.

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100. Stipulation and Agreement of Compromise, Settlement, and Release, *supra* note 97, at 6.

101. *Trulia*, 129 A.3d at 889–90.

102. FED. R. CIV. P. 23(b) (explaining that classes, by their nature, must include and bind all affected individuals to avoid inconsistency that would arise from individual litigation).

103. *In re Caremark Int'l Inc. Derivative Litig.*, 698 A.2d 959, 966–67 (Del. Ch. 1996) (“[T]he Court attempts to protect the best interests of the corporation and its absent shareholders all of whom will be barred from future litigation on these claims if the settlement is approved.”).

104. FED. R. CIV. P. 23(e); *see also* DEL. CH. CT. R. 23(e).

105. *Trulia*, 129 A.3d at 907.

However, Chancellor Bouchard's review found that the additional disclosures that the Trulia board provided were immaterial, and therefore, the settlement was based on consideration that had no value.<sup>106</sup> The additional information Trulia offered was obviously massaged from the existing disclosures, if not downright trivial. In any event, none of the information submitted could have been expected to affect a stockholder's decision to approve the merger.<sup>107</sup> With the disclosures deemed "immaterial,"<sup>108</sup> they could not serve as consideration for the release of claims the stockholder class would give in exchange.<sup>109</sup> With no approved settlement, the court had no basis on which to approve attorney's fees.<sup>110</sup>

In rejecting the parties' settlement proposal, Chancellor Bouchard adopted a "plainly material" standard that the court will apply to all disclosures offered as consideration for a release of claims in merger objection litigation.<sup>111</sup> This effectively brought disclosure assessment under Delaware corporate law in line with disclosure assessment under the federal securities laws as amended by the PSLRA.<sup>112</sup> Since Delaware plaintiffs' "hastily drafted complaints" seeking throw-away disclosures will now be subject to greater scrutiny than before,<sup>113</sup> the practice of collecting six-figure attorney's fee awards<sup>114</sup> for relatively little effort has suddenly become much less of a certainty for plaintiffs'

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106. *Id.*

107. *Id.* at 904–05 (explaining that one additional disclosure merely added "additional minutiae underlying some of the assumptions" in the original disclosures, while another was just a "triviality [that] could not reasonably be expected to affect the total mix of information").

108. *Id.* at 905 (quoting *In re MONY Grp. Inc. S'holder Litig.*, 852 A.2d 9, 28 (Del. Ch. 2004)).

109. *Id.* at 907.

110. *See generally id.*

111. *Id.* at 898.

112. 15 U.S.C. § 78u-5(c)(1)(A) (2012) (class actions cannot prevail unless disclosed information was materially false).

113. *Trulia*, 129 A.3d at 892.

114. *See* ROBERT M. DAINES & OLGA KOUMRIAN, CORNERSTONE RESEARCH, SHAREHOLDER LITIGATION INVOLVING MERGERS AND ACQUISITIONS: REVIEW OF 2012 M&A LITIGATION 9 (Feb. 2013 Update) [hereinafter CORNERSTONE 2012] (average fee requested in 2012 was \$540,000); Phillip R. Sumpter, *Adjusting Attorneys' Fee Awards: The Delaware Court of Chancery's Answer to Incentivizing Meritorious Disclosure-Only Settlements*, 15 U. PA. J. BUS. L. 669, 703–04 (2013) (Sumpter conducted an empirical study that grouped fee awards into three bands, with the majority of Delaware settlements approved awarding fees in the \$300,000 to \$500,000 award band, while Vice Chancellor Laster repeatedly argued that the \$400,000 to \$500,000 award band is the appropriate starting-off point).

lawyers.<sup>115</sup> In raising the standard and making settlements and quick fee payouts more difficult to secure, the *Trulia* decision should (and recent data suggests that it already has) serve as a deterrent to overenforcement of Delaware corporate law.<sup>116</sup> Zealous plaintiffs' lawyers will be less likely to challenge deals in Delaware court, and this has the potential to free up hundreds of millions of dollars in corporate resources, which ultimately benefits stockholders.<sup>117</sup>

Considering the scope of abusive disclosure-only settlement litigation, the *Trulia* standard has the potential to reduce vexatious corporate litigation, which is itself an extension of federal securities litigation. *Trulia* offers a ready tool for state court judges to apply in corporate litigation. Nevertheless, because of the strong nexus to the federal securities laws, federal judges should also look to *Trulia*'s materiality standard when considering inadequate securities disclosure claims.

#### V. TRULIA'S RELEVANCE TO THE FEDERAL SECURITIES LAWS

##### A. *At Its Heart, Trulia Is a Federal Securities Law Decision*

Even though *Trulia* is a state corporate law decision, it can and should be applied by federal judges hearing federal securities law claims. *Trulia* is relevant because it rests entirely on questions that are endemic to federal securities laws governing public disclosures.

As noted earlier, the plaintiffs in *Trulia* brought four separate claims.<sup>118</sup> The first three claims arose under Delaware corporate law, while the fourth claim alleging deficient public disclosures with the SEC was a question squarely rooted in the federal securities laws. The

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115. See CORNERSTONE 2016, *supra* note 66, at 2. Merger litigation fell to only 64% of announced deals in the first half of 2016, down from 84% in 2015, *id.*, and 93% in 2012. CORNERSTONE 2012, *supra* note 114, at 1.

116. See CORNERSTONE 2016, *supra* note 66, at 1 (noting the reduction of merger litigation in the first half of 2016 and attributing this to *Trulia*).

117. Amanda M. Rose, *Reforming Securities Litigation Reform: Restructuring the Relationship Between Public and Private Enforcement of Rule 10B-5*, 108 COLUM. L. REV. 1301, 1313 (2008) (describing the equal application both in the context of 10b-5 securities class actions and merger objection class actions, of the concept of "pocket shifting"—the idea that the members of a class-action suit are likely to be shareholders, thus a judgment against the corporation actually hurts them).

118. *Id.* at 888–89.

only response to these four claims by the defendant was to issue additional disclosures; however, the information in the additional disclosures did not resolve the first three corporate law claims.<sup>119</sup> Even though the plaintiffs never amended their pleading to withdraw these three claims, the proposed settlement referenced only the additional disclosures and attorney's fees.<sup>120</sup> Chancellor Bouchard did not even directly address the other claims sounding in corporate law. In other words, corporate law claims, germane to Delaware law and properly at home in the Court of Chancery, were ignored, while claims based in securities law and most appropriately heard in federal court, dominate the decision. This supports the idea that disclosure-only merger litigation is actually federal securities litigation dressed in disguise to allow it to escape federal jurisdiction.

This practice has become commonplace. Sometimes the judge hearing the case glosses over the perfunctory corporate law claims; other times, the plaintiffs themselves move quickly past these claims towards a disclosure-based settlement.<sup>121</sup> In *Trulia*, Chancellor Bouchard did not afford any attention to the plaintiffs' three corporate law claims, instead focusing his decision entirely on the inadequate disclosure claim, a claim at home under the federal securities laws.<sup>122</sup>

Why might Chancellor Bouchard ignore the other three outstanding claims? One possible explanation is that he knew that these claims were essentially throwaways and that raising such claims, only to later withdraw all but a deficient disclosure claim, was common practice in the Court of Chancery.<sup>123</sup> It could be that the practice of

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119. *See id.*

120. *Id.* at 889–90.

121. *See In re Sauer-Danfoss Inc. S'holders Litig.*, 65 A.3d 1116, 1119–20 (Del. Ch. 2011). In *In re Sauer-Danfoss*, the original claims included inadequate price and breach of fiduciary duty by Danfoss for announcing intention to proceed with a tender offer, and by Sauer-Danfoss for responding to the proposed tender offer. *Id.* After filing the suit, no attempt was made for relief on these claims; rather, the parties went straight to disclosure-only settlement talks. *Id.*; *see also In re Transatlantic Holdings Inc. S'holders Litig.*, C.A. No. 6574-CS, 2013 WL 1191738, at \*3 (Del. Ch. Mar. 8, 2013) (“[A] suit without any real investigation or depth was immediately traded away by the plaintiffs for simply more information which did not contradict the mix of information that was already available.”).

122. *In re Trulia, Inc. Stockholder Litig.*, 129 A.3d 884, 899–907 (Del. Ch. 2016).

123. *Id.* at 892 (Bouchard, C.) (explaining that there are “regular players . . . routinely filing hastily drafted complaints . . . on the heels of the public announcement of a deal and



loading a complaint with meritless claims, only to later withdraw all but the inadequate disclosure claim, had grown commonplace and perfunctory, and the Chancellor simply did not bother to comment on the oversight. Whatever the reason, the Chancellor's neglect even to engage the questions of corporate law and his focus only on the question of the inadequacy of federal securities disclosures shows that the decision in *Trulia* is ripe for application by federal judges hearing securities law claims.

*B. Exporting Trulia: A Precedent to Shore Up Private Enforcement in Securities Litigation*

*Trulia* is shaping up to be a watershed decision in public merger litigation. Because Delaware “dominates the market for incorporations of publicly traded firms”<sup>124</sup> and is renowned for its expertise in corporate matters,<sup>125</sup> the law and policy that the Court of Chancery develops has a disproportionately large influence on corporate law nationwide.<sup>126</sup> In fact, Chancellor Bouchard's declaration in *Trulia* that disclosure-only settlements would be rejected unless the disclosures offered material information to stockholders<sup>127</sup> has since taken firm root in several other jurisdictions.

Within months of the ruling, four more Court of Chancery decisions followed Chancellor Bouchard's holding in *Trulia*,<sup>128</sup> and four non-Delaware state court decisions had applied it or cited it

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settling quickly on terms that yield no monetary compensation to the stockholders they represent”).

124. Sara Lewis, *Transforming the “Anywhere but Chancery” Problem into the “Nowhere but Chancery” Solution*, 14 STAN. J.L. BUS. & FIN. 199, 200 (2008).

125. John Armour et al., *Delaware's Balancing Act*, 87 IND. L.J. 1345, 1381 (2012) (explaining that Delaware courts are the “standard-setter for corporate law”).

126. See *In re Walgreen Co. Stockholder Litig.*, 832 F.3d 718, 725 (7th Cir. 2016) (Posner, J.) (encouraging federal judges to adopt policy developed in the Court of Chancery because of that forum's familiarity with “large transactions by public companies”); Latham & Smith III, *supra* note 87.

127. *Trulia*, 129 A.3d at 898–99.

128. See *In re Merge Healthcare Inc., Stockholders Litig.*, Consol. C.A. No. 11388-VCG, 2017 Del. Ch. LEXIS 17, at \*27–28 (Del. Ch. Jan. 30, 2017); *Nguyen v. Barrett*, C.A. No. 11511-VCG, 2016 Del. Ch. LEXIS 147, at \*9 (Del. Ch. Sept. 28, 2016); *In re Xoom Corp. Stockholder Litig.*, Consol. C.A. No. 11263-VCG, 2016 Del. Ch. LEXIS 117, at \*9 (Del. Ch. Aug. 4, 2016); *La. Mun. Police Emps.' Ret. Sys. v. Black*, C.A. No. 9410-VCN, 2016 Del. Ch. LEXIS 36, at \*19–20 (Del. Ch. Feb. 19, 2016).

favorably.<sup>129</sup> Perhaps most importantly, Judge Richard Posner, writing for the United States Court of Appeals for the Seventh Circuit, followed *Trulia* in *In re Walgreen*.<sup>130</sup> Posner prefaces his application of *Trulia* by saying that “Delaware’s Court of Chancery sees many more cases involving large transactions by public companies than the federal courts of [the Seventh] [C]ircuit do, and so we should heed” Chancellor Bouchard’s decision.<sup>131</sup> He then adopted, and quoted at length, Chancellor Bouchard’s “plainly material” standard for supplemental disclosure settlements.<sup>132</sup> Even prior to *Trulia*, other courts had begun to push back on meritless disclosure-only settlements.<sup>133</sup>

While the increasing adoption of the *Trulia*’s “plainly material” standard in state and federal court is encouraging, it is not universal. In New York, for example, the courts have moved away from a materiality standard. In 2014, the New York Supreme Court, hearing *Gordon v. Verizon Communications*, analyzed whether a disclosure-only settlement offered shareholders any “material value.”<sup>134</sup> This standard foreshadowed *Trulia*. But then in 2017, the Supreme Court Appellate Division for the First Department in New York reversed the decision in *Gordon*, applying instead a “some benefit” standard.<sup>135</sup> *Gordon* seems to stand for the clear rejection of *Trulia*’s “plainly

129. See *In re Am. Capital, Ltd. S’holder Litig.*, No. 422589-V, 2016 Md. Cir. Ct. LEXIS 6, at \*31 n.51 (Cir. Ct. Md. Oct. 6, 2016); *Corwin v. British Am. Tobacco PLC*, No. 14 CVS 8130, 2016 NCBC LEXIS 14, at \*11–12 (N.C. Super. Ct. Feb. 17, 2016); *Strougo v. N. State Bancorp*, No. 15 CVS 14696, 2016 NCBC LEXIS 13, at \*3 (N.C. Super. Ct. Feb. 16, 2016); *Raul v. Burke*, No. 15 CVS 16703, 2016 WL 382833, at \*1 n.2 (N.C. Super. Ct. Jan. 28, 2016).

130. *In re Walgreen*, 832 F.3d at 725.

131. *Id.*

132. *Id.*

133. See *City Trading Fund v. Nye*, No. 651668/2014, 2015 WL 93894, at \*13 (N.Y. Sup. Ct. Jan. 7, 2015) (quoting *In re Cogent, Inc. S’holder Litig.*, 7 A.3d 487, 509 (Del. Ch. 2010)) (“None of the supplemental disclosures ‘significantly altered the total mix’ of information made available.”), *rev’d*, 43 N.Y.S.3d 21 (N.Y. App. Div. 2016); *Gordon v. Verizon Commc’ns, Inc.*, No. 653084/13, 2014 WL 7250212, at \*3 (N.Y. Sup. Ct. Dec. 19, 2014) (stating additional disclosures “add[ed] nothing of material value”), *rev’d*, 46 N.Y.S.3d 557 (N.Y. App. Div. 2017).

134. *Gordon*, 2014 WL 7250212, at \*3.

135. *Gordon v. Verizon Commc’ns, Inc.*, 46 N.Y.S.3d 557, 571 (N.Y. App. Div. 2017), *rev’g* *Gordon v. Verizon Commc’ns, Inc.*, No. 653084/13, 2014 WL 7250212, at \*3 (N.Y. Sup. Ct. Dec. 19, 2014).

material” standard.<sup>136</sup> As one commentary describes, since *Trulia*, “actions are being filed in one (or more) states other than Delaware or in federal courts . . . courts in a variety of jurisdictions with less experience than the Court of Chancery are adjudicating these cases, which may result in less consistency in connection with the settlement of these actions.”<sup>137</sup>

The clarity of Chancellor Bouchard’s standard for settlement approval in *Trulia* and the influence of Delaware decisions in corporate law nationally have the potential to make positive inroads towards curbing abusive public merger litigation.<sup>138</sup> In fact, recent data suggests that *Trulia* has kicked off a shift in merger litigation trends. A 2016 study from Cornerstone Research analyzing trends in merger litigation documented “substantial” declines in merger objection litigation following *Trulia*.<sup>139</sup> The authors of the report suggested that *Trulia* may be to blame (or perhaps more accurately to thank) for this.<sup>140</sup> However, in its 2017 report, Cornerstone reported new data showing that merger litigation in federal courts had increased in the first half of 2017 to the highest level since 2009.<sup>141</sup> It is possible that the initial decline in merger litigation reported in 2016 was simply a lull as plaintiff’s lawyers redrew their litigation strategy. In any event, it seems clear that *Trulia* “caused plaintiffs to shift merger objection litigation to federal court.”<sup>142</sup> What recent data around the uptick in merger litigation in federal courts, and what New York’s unfortunate decision to adopt a litigation-baiting “some benefit” standard make

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136. Michael Maimone & Joseph Schoell, *Chancery Should Reconsider Its Decision in Trulia*, LAW 360 (May 9, 2017, 10:34 AM EDT), <https://www.law360.com/articles/921686/chancery-should-reconsider-its-decision-in-trulia>.

137. *Id.*

138. *See In re Walgreen Co. Stockholder Litig.*, 832 F.3d 718, 723 (7th Cir. 2016) (“*Trulia* adopted a clearer standard for the approval of such settlements.”).

139. CORNERSTONE 2016, *supra* note 66, at 2 (“The rate of M&A litigation has declined substantially since the Delaware Court of Chancery’s decision in *Trulia*.”).

140. *Id.* at 1 (“The lower rate [of merger litigation] in late 2015 and the first half of 2016 may be due to the impact of the January 2016 *Trulia* ruling that diminished the acceptability of disclosure-only settlements.”).

141. CORNERSTONE RESEARCH, SECURITIES CLASS ACTION FILINGS: 2017 MIDYEAR ASSESSMENT 1 (2017).

142. *Id.*

clear is the need for state and federal judges to join Judge Posner in uniformly adopting *Trulia*'s "plainly material" standard.

Empirical evidence suggests that Delaware's approach works to dissuade abusive litigation. Beginning in 2015, when Delaware judges started refusing to approve disclosure-only settlements, and culminating with *Trulia* in early 2016, the rate of merger litigation in Delaware declined significantly.<sup>143</sup> The resurgence of merger litigation in federal court since then suggests that the plaintiff's bar now has a bleaker outlook on the prospects of success in Delaware and is seeking softer targets. A judicial standard of plain materiality, hatched in Delaware state court and applied across the country in state and federal court, has the potential to apply downward pressure to all disclosure-based merger litigation, regardless of forum. However, in order to avoid forum arbitrage and the inevitable race to the bottom that disparate standards encourage, the standard must be universal. A united stand against meritless disclosure settlements has the potential to reduce abusive merger litigation and restore efficiency to the system of private enforcement of securities-based law.

## VI. CONCLUSION

Any analysis of the effectiveness of private enforcement of the federal securities laws is incomplete without also taking into consideration the spillover of securities litigation into state courts under the guise of corporate law claims beginning in the 1990s.

For years, private litigation enforcing federal securities laws has been plagued by abuse. Congress's legislative fixes in the mid-1990s and 2000s ended up pushing the problem into state courts under the guise of corporate fiduciary claims. The heart of the problem, however, remained unchanged: the ease of bringing class-action lawsuits built on information readily available in federal securities filings, and the relative certainty of a corporate defendant anxious to settle. Chancellor Bouchard changed this dynamic. He introduced a "plainly material" standard to the disclosure-only settlement approval process. The direct result is that parties to disclosure-based merger litigation can no longer settle meritless claims simply by producing

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143. Steven Davidoff Solomon, *Why the Surge in Merger Litigation Fizzled*, N.Y. TIMES: DEAL BOOK, Jan. 22, 2016), <https://www.nytimes.com/2016/01/23/business/dealbook/why-the-surge-in-merger-litigation-fizzled.html>.

unhelpful additional disclosures and paying attorneys' fees. This tactic, long used by plaintiffs' lawyers because of its quick and relatively low-effort route to a substantial paycheck, seems to have lost these most appealing characteristics. The indirect result of Chancellor Bouchard's decision has been an immediate and continued decline in merger litigation in Delaware. If this new standard is indeed responsible for scaring off meritless claims in Delaware, and the evidence suggests that it is, then this speaks well for private litigation as a tool for efficiently enforcing the federal securities laws. What remains to be seen is how the rest of the country will respond. As plaintiff's lawyers seek out new fora for these merger strike suits, it will be up to state and federal judges to adopt and apply *Trulia's* "plainly material" standard. Already, *Trulia* is being considered in judicial decisions outside of Delaware, in most cases with eager acceptance, but in others with skepticism. A uniform application of the *Trulia* standard is needed. A unified application of the "plainly material" standard in class-action settlement review will reduce abusive securities-based litigation. The result will be increased efficiency of private litigation as an enforcement mechanism for claims based in the federal securities laws.

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