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An Oversight Claim By Any Other Name Is Reviewed Under 'Caremark,' Says GoPro

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Plaintiffs are eager to convert every corporate trauma into derivative claims, but they are anything but eager to confront the exacting standards for pleading and proving bad faith oversight under *Caremark*. Under *Caremark* and its progeny, directors are liable for failing to prevent corporate harm only under egregious circumstances in which they *knowingly* allow a corporation to violate or continue violating the law. Delaware courts routinely dismiss *Caremark* claims and have repeatedly emphasized that bad faith oversight is "possibly the most difficult theory in corporation law upon which a plaintiff might hope to win a judgment."

So what is a plaintiff to do? In *In re GoPro, Inc. Stockholder Derivative Litigation*, C.A. No. 2018-0784-JRS (Del. Ch. Apr. 28, 2020), the plaintiffs recast their challenges to director oversight as challenges to director *decisions* and denied they were asserting *Caremark* claims. Vice Chancellor Slights was not convinced. He dismissed the claims under the theory the plaintiffs urged and under *Caremark* as well. "Although the plaintiffs disclaim any effort to plead a *Caremark* claim," Slights observed, "it is difficult to ignore the allegations in the Complaint that walk and talk like *Caremark*." *GoPro* adds to a growing body of cases that reject attempts to sidestep *Caremark* by portraying director oversight that falls short of preventing some corporate harm as affirmative misconduct instead.

The claims in *GoPro* arose from the company's failure to meet its annual revenue projection for 2016, due to setbacks with a new drone product the company was marketing. After the company announced the disappointing results, its stock price declined. Stockholders filed a securities class action alleging that the company and its officers "knew the company could not meet its annual revenue guidance yet failed timely to disclose this reality to stockholders." After the securities class action was filed, other stockholders filed derivative suits claiming that GoPro's directors and officers breached their fiduciary duties to the company on the same theory. Having failed to make a pre-suit demand, the derivative plaintiffs argued that demand was futile because "a majority of the demand board face a substantial likelihood of liability for authorizing or failing to prevent the alleged misstatements."

Typically, claims that directors are liable for not preventing corporate harm are analyzed under *Caremark*, but the plaintiffs strained to avoid that analysis by arguing that they challenged the directors' decisions to *cause* the company to make false statements, rather than their oversight. The plaintiffs further argued that *Caremark* should not apply because the directors allegedly "contributed to and approved GoPro's revenue guidance while knowing it was impossible the company to achieve the projected results."

The court rebuked this pleading tactic. As it explained,

> The complaint begins its narrative by leaving a breadcrumb trail that appears to lead to a claim of oversight liability under *Caremark*. But then the trail runs cold as the plaintiffs disclaim any attempt to plead a failure of board oversight. Then, just as the reader is

> about to fire the "help me I'm lost" flare, the complaint pivots to assert a claim of malfeasance by virtue of the Board's role in actively causing GoPro to release false and misleading statements to its stockholders and the market.

Such artful pleading, the court observed, undermines the credibility of allegations that demand is futile. The plaintiffs are, of course, permitted to plead alternative theories, but to overcome the demand requirement, they must plead demand futility with factual particularity. "[W]hen the plaintiff struggles consistently to characterize the nature of the underlying wrongful conduct that gives rise to his claims, this imprecision signals that he may not have pleaded such conduct *with particularity*."

The court also categorically rejected the plaintiffs' argument that claiming the directors *knew* about the supposedly false statements removes their case from *Caremark* analysis. As the court explained, director knowledge does not transform "board *acquiescence*" reviewed under *Caremark* into "*affirmative* board-level misconduct":

> Even if the board were told by its management that the company was not going to meet its revenue projections, and then did nothing as management publicly stood by its market guidance, that factual predicate would support a "classic" *Caremark* claim for failure to respond to "red flags," not a claim against the board for causing the company to make false disclosures.
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> That is because a director's alleged failure to take action in response to "actual knowledge" of wrongdoing is not a distinction from *Caremark*, but rather the fundamental premise of *Caremark* liability. If the plaintiffs had been correct that knowledge of wrongdoing renders *Caremark* inapplicable, then *Caremark* would be inapplicable to the only cases in which there could be oversight liability.

After dispensing with the plaintiffs' affirmative misconduct theory, the court went on to evaluate the claims under traditional *Caremark* analysis and ruled that the complaint failed to plead specific allegations that the board knew the company's projections were false. The court rejected, among other arguments, the plaintiffs' contention that such knowledge could be inferred merely because the board had access to a database system that allegedly could have revealed inventory shortages of GoPro's drone product. "Taking a self-guided tour through [the] system to check inventory levels for a product that would comprise only 10% of the company's revenue," the court concluded, "is not the sort of 'oversight' *Caremark* contemplates." The court further rejected claims that the demand was futile because the board lacked independence or because just one of its directors was named a defendant in the parallel securities suit and allegedly sold shares before the company's stock price declined. The court, thus, dismissed the complaint for failure to make a demand.

GoPro highlights a growing trend: plaintiffs are increasingly seeking shelter from *Caremark*'s demanding standard of liability by trying to reframe their challenges to director oversight as challenges to supposed decisions to allow some corporate injury to occur. *GoPro* also illustrates that the resulting metaphysical debate about the difference between the action and inaction of directors serves only to complicate briefing; it makes no real difference in legal analysis or outcomes. For starters, Delaware courts see through these semantics. If the gravamen of a claim is that the board should have prevented something from happening, Delaware courts will generally apply *Caremark*. Furthermore, the burden of plaintiffs to plead and prove bad faith is materially the same whether an injury to a corporation resulted from something a board did or something it did not do. At least when a corporation has adopted an exculpatory charter provision under 8 *Del. C.* Section 102(b)(7) (as most have), directors are liable only when they knowingly engage in wrongdoing themselves or when knowingly allow a corporation to violate the law. The buck the stops at culpable knowledge—no matter how the claims are framed.

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