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Securities Litigation Landscape Continues to Evolve as 1933 Act Filings Reach All-Time High

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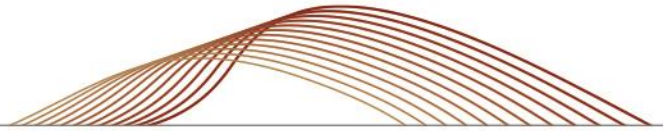
In March 2018, in *Cyan, Inc. v. Beaver County Employees Retirement Fund,*[1] the Supreme Court held that state courts have concurrent subject matter jurisdiction over actions that exclusively allege claims under the Securities Act of 1933 ("Securities Act" or "1933 Act"). Many commentators and practitioners predicted that *Cyan* would result in a surge of Securities Act claims brought in state courts, where the procedural rules are perceived to be more plaintiff-friendly. Thus far, that prediction has held true.

There were, according to Cornerstone Research Inc., sixty-five (65) federal and state court actions filed in 2019 alleging claims under the Securities Act—an increase of nearly 60 percent from 2018.[2] This rise in activity was driven in part by an increase in filings in New York state court that, for the first time, eclipsed those in California, the state where plaintiffs frequently pursued Securities Act lawsuits prior to *Cyan.*[3] In addition, filings in state courts outside of New York and California last year almost ***tripled*** as compared to 2018.[4]

We previously wrote about several significant post-*Cyan* New York state decisions during the first half of 2019 (https://www.law360.com/articles/1182662/4-ny-cases-forge-post-cyan-securities-litigation-landscape). In those decisions, we discussed, among other things, the New York Supreme Court's application of federal securities law precedents to dismiss Securities Act claims at the pleading stage. We also analyzed cases where New York courts refused to issue a stay in favor of federal proceedings and reached differing conclusions on whether the automatic discovery stay under the Private Securities Litigation Reform Act of 1995 ("PSLRA") applies in state court. This article continues that discussion by looking at additional notable rulings from the second half of 2019 and early 2020 as state court Securities Act jurisprudence continues to develop.

Pitney Bowes, Inc. **Securities Litigation (Connecticut Superior Court)[5]**

In *Pitney Bowes*, plaintiff filed a purported class action asserting claims under Sections 11, 12, and 15 of the Securities Act on behalf of purchasers in the September 2017 IPO of Pitney Bowes, Inc., a global technology company. Plaintiff claimed the IPO offering materials were false and misleading because they failed to disclose declines in Pitney Bowes' largest earning business segment (Small and Medium Business Solutions (SMB)) and their corresponding effects on the company's financial performance.[6] Applying federal securities precedent, Judge Charles T. Lee granted defendants' motion to strike the complaint in its entirety for, among other things, failure to plead any material misstatement or omission.[7]



Failure to Allege Known Trends or Uncertainties Under Item 303. Item 303 requires, among other things, that an issuer describe "any known trends or uncertainties that have had or that the registrant reasonably expects will have a material favorable or unfavorable impact on net sales or revenues or income from continuing operations."[8] The failure to disclose information subject to Item 303 of SEC Regulation S-K provides a basis for liability under the Securities Act.

The Court held that the complaint did not establish any basis for liability under Item 303. Specifically, plaintiff failed to allege any "uncertainties" because defendants were allegedly "fully aware" of the impact that declining sales and margins in the SMB segment had on the company's overall business.[9] The purported declines also did not constitute a "trend" because there was nothing in the complaint suggesting they were part of an "ongoing pattern" and were alleged to have taken place only during the third quarter of 2017, when the IPO occurred.[10]

Alleged Omissions Did Not Render Disclosures Misleading. The Court also found that Pitney Bowes' failure to disclose information about the purported declines did not render any statements in the offering materials misleading. Judge Lee explained that the alleged misstatements—which concerned a "high level of recurring revenue" and improvements in equipment sales and margins in the SMB business—were "accurate statements of historical fact."[11] They did not carry any promise of future performance and were not misleading due to defendants' failure to disclose the purported Q3 2017 declines.[12]

In re Greensky, Inc. Securities Litigation (New York Supreme Court)[13]

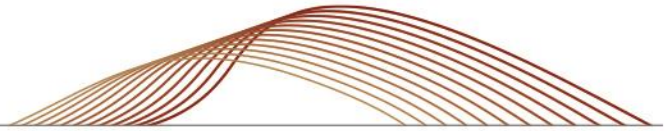
In *Greensky,* plaintiffs brought Section 11, 12(a)(2), and 15 claims relating to allegedly false and misleading statements made in connection with the IPO of GreenSky, Inc., a financial technology company. Defendants sought a stay of the state action in favor of a later-filed federal proceeding or, alternatively, a stay of discovery until determination of defendants' motion to dismiss pursuant to the PSLRA. Judge Jennifer G. Schecter denied the motion to stay the action, but granted a stay of discovery pending a decision on defendants' motion to dismiss.

Denial of Motion to Stay State Court Action. The Court held that New York State was plaintiffs' first choice of forum, and there was "no basis" for a stay in favor of the federal proceeding. Judge Schecter explained that staying state court litigation "without a compelling reason to do so" would undermine the principle set forth in *Cyan,* namely that "state courts can preside over 1933 Act cases" and such actions cannot be removed to federal court.[14]

Stay of Discovery Pending Defendants' Motion Dismiss. Despite denying defendants' motion to stay the state court action, Judge Schecter found that the "important purpose underlying enactment of the [PSLRA's] automatic stay [of discovery]—ensuring that cases have merit at the outset—should not be disregarded merely because a federal cause of action is being prosecuted in state court." Accordingly, the Court held that it was "appropriate to give effect to the PSLRA's policy" and granted defendants' motion to stay discovery pending a determination on the motion to dismiss.[15]

In re NIO Inc. Securities Litigation (New York Supreme Court)[16]

Like *Greensky,* the New York Supreme Court in *NIO* faced a motion to stay the state action in favor of a similar federal proceeding, but reached the opposite result. Judge Barry S. Ostrager found that, although the state lawsuit was "more advanced" than the federal proceeding, the federal action was the first filed and had the potential to resolve both the Securities Act claims, as well as claims under



the Exchange Act brought solely in federal court.[17] Accordingly, the Court granted defendants' motion to stay the state court action, without prejudice, in favor of the federal proceeding.[18]

Mahar v. General Electric Co. (New York Supreme Court)[19]

In *Mahar,* the New York Supreme Court again granted a motion to stay the state Securities Act lawsuit in deference to an earlier-filed federal proceeding. Notably, however, there was no overlap in the claims across the proceedings—the federal action asserted claims solely under the Exchange Act, while the state action asserted Securities Act violations. Judge Andrew Borrok found the differing legal theories to be "inconsequential" and explained that the "hallmark for a stay under First Department law is that both actions recover for the same alleged harm based on the same underlying events."[20] Accordingly, Judge Borrok held that a stay of the state action was warranted, since the federal and state proceedings arose out of the same "series of alleged wrongs," involved "substantially the same parties," and sought "substantially the same relief."[21]

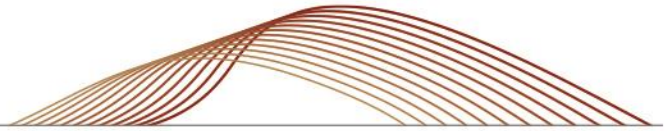
Venator Materials PLC Securities Litigation (Texas Court of Appeals)[22]

Plaintiffs in *Venator* brought Securities Act claims in connection with two securities offerings of Venator Materials, a manufacturer of chemical products. Plaintiffs claimed that the offering materials were false and misleading because they failed to disclose the extent of damage caused by a fire in one of Venator's manufacturing plants in Finland, and its effect on the company's ability to produce its primary chemical product, titanium dioxide. The named defendants included the company, certain of its officers and directors, and the underwriters of the offerings. The Texas Court of Appeals overturned a decision of the trial court and dismissed the case against these defendants for lack of personal jurisdiction.[23]

Lack of General Jurisdiction. The Court found that Venator (a U.K. company) and the underwriters (which were each incorporated and had its principal place of business outside of Texas) were not "at home" in Texas and not subject to general jurisdiction in the state.[24] Similarly, the court lacked general jurisdiction over the individual defendants, who the Court found were each domiciled in the United Kingdom.[25]

Lack of Specific Jurisdiction. The Court also held that it lacked specific jurisdiction, because there was not a "substantial connection" between any of the defendants' contacts with Texas and the operative facts of the litigation. The Court found, among other things, that the alleged misrepresentations and omissions were about events and actions that took place outside of Texas, namely the fire and subsequent investigation (which occurred in Finland), and the company's titanium dioxide business (which was conducted from the UK).[26] In addition, the offering materials, which were prepared by New York or Delaware underwriters, were directed to "regulators in Washington, D.C. and to potential investors nationwide—rather than as a purposeful availment of" conducting activities within Texas.[27]

The Texas Court of Appeals also rejected plaintiffs' argument that there was specific jurisdiction over the underwriters, based on their underwriting agreement with Venator and its predecessor companies, certain of which were based in Texas. The Court held that the underwriters "specifically structured" their agreement—which contained New York choice of law and venue provisions and required performance (i.e., payment of the purchase price and delivery of stock certificates) at a specified address in New York—so as "neither to profit from [Texas'] laws nor be subject to its jurisdiction."[28]



Nationwide Service of Process Provision Does Not Confer Jurisdiction. The Texas Court of Appeals also rejected plaintiffs' argument that Section 22(a) of the Securities Act provides an alternative basis for jurisdiction. Section 22(a) allows for nationwide service of process, which effectively provides federal courts with personal jurisdiction in a Securities Act case over any defendant that either resides in or has sufficient contacts with the United States.[29] Following decisions of state courts in Delaware and West Virginia, the Texas Court of Appeals held that this nationwide service of process provision does not apply in state court proceedings.[30]

Ramifications

These decisions represent important additions to the developing collection of state law jurisprudence addressing Securities Act claims.

First, the *Pitney Bowes* decision further illustrates that, as discussed in our prior alert, application of federal securities law precedents and related regulations (such as Item 303) can be just as effective in state court as federal court to dismiss deficient Securities Act claims.

Second, the Greensky decision represents yet another addition to the growing divide on whether the PSLRA discovery stay applies in state courts—an issue that has split courts of different states and courts in New York, including those within New York County.[31] Plaintiffs and defendants alike will continue to monitor these decisions closely until appellate courts weigh in and decide this important issue.

Third, *NIO* is important precedent for defendants who confront parallel state and federal court proceedings. Several state court rulings have denied motions to stay in deference to later-filed federal court proceedings. While in *NIO* the federal action was first-filed, it was "roughly contemporaneous" with the state court action and not the only factor the Court considered in staying the state court litigation. Importantly, the Court also took note of the fact that the federal court action had additional Exchange Act claims that could be resolved together with the Securities Act claims in a single federal forum. Similarly, *Mahar* is helpful authority for defendants who are seeking a stay of state proceedings, even when the parallel federal action is based entirely on different legal claims.

Finally, the *Venator* decision serves as an important reminder that, although plaintiffs have the ability to pursue Securities Act claims in state court, defendants can potentially seek dismissal on the basis of lack of personal jurisdiction when their contacts with the forum state are insufficient to support general or specific jurisdiction.

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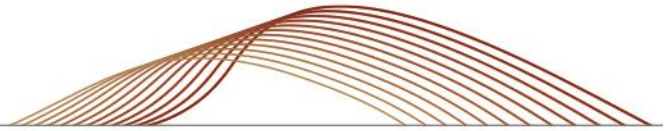

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[1] 138 S. Ct. 1061 (2018).
[2] Cornerstone Research, *Securities Class Action Filings: 2019 Year in Review*, 1, 25 (2020), https://www.cornerstone.com/Publications/Reports/Securities-Class-Action-Filings-2019-Year-in-Review.
[3] *Id.* at 19.
[4] *Id.* (noting these filings were in Florida, Illinois, Massachusetts, Michigan, Nevada, New Jersey, Pennsylvania, Rhode Island, Tennessee, Texas, and Wisconsin).
[5] *City of Livonia Retiree Health and Disability Benefits Plan v. Pitney Bowes, Inc.,* Superior Court, Judicial District of Stamford, Complex Litigation Docket, Docket No. X08-CV-18-6038160-S (#146) (Oct. 24, 2019).
[6] *Id.* at 2.
[7] Since plaintiff failed to allege any direct purchase of the securities at issue from an underwriter defendant, the Section 12 claim against the underwriters was dismissed for lack of standing. *See City of Livonia Retiree Health and Disability Benefits Plan v. Pitney Bowes, Inc.,* Superior Court, Judicial District of Stamford, Complex Litigation Docket, Docket No. X08-CV-18-6038160-S (#149) at 4-5 (Oct. 24, 2019).
[8] SEC Regulation S-K, 17 C.F.R. § 229.303(a)(3)(ii).
[9] *City of Livonia,* No. X08-CV-18-6038160-S (#146) at 10-11.
[10] *Id.* at 11-15.
[11] *Id.* at 15-19.
[12] *Id.*
[13] *In re Greensky, Inc. Sec. Litig.,* No. 655626/2018, 2019 WL 6310525 (N.Y. Sup. Ct., N.Y. Cty., Nov. 25, 2019).
[14] *Id.* at *2.
[15] *Id.* at *3, 4.
[16] *In re NIO Inc. Sec. Litig.*, Index No. 653422/2019 (N.Y. Sup. Ct., N.Y. Cty., Dec. 13, 2019) (Ostrager, J.).
[17] *Id.* at 1.
[18] *Id.*
[19] *Mahar v. General Electric Co.,* 65 Misc. 3d 1121 (N.Y. Sup. Ct., N.Y. Cty., Oct. 15, 2019).
[20] *Id.* at 1132.
[21] *Id.* at 1131.
[22] *Venator Materials PLC v. Macomb Cty. Emps' Ret. Sys. & Firemen's Ret. Sys. of St. Louis,* No. 05-19-01177-CV, 2020 WL 289296 (Tex. App. Jan. 21, 2020).
[23] The case against the remaining defendants (who did not challenge jurisdiction) was remanded to the trial court for a transfer of venue to Montgomery County, Texas. *Id.* at *17-18.
[24] *Id.* at *2, 8-9, 14.
[25] *Id.* at *9-13.
[26] *Id.* at *10.
[27] *Id.*
[28] *Id.* at *14-16.
[29] *Balestra v. ATBCOIN LLC,* 380 F. Supp. 3d 340, 348-49 (S.D.N.Y. 2019).
[30] *Venator Materials*, 2020 WL 289296, at *11-12.
[31] *See* Kevin Broughel, Anthony Antonelli, and Amanda Pober, *4 NY Cases Forge Post-Cyan Securities Litigation Landscape*, LAW360 (Aug. 29, 2019), https://www.law360.com/articles/1182662/4-ny-cases-forge-post-cyan-securities-litigation-landscape.