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TWO AREAS FOR REFORM IN SECURITIES LITIGATION

Securities litigation has increased dramatically in recent years. Taking note of this, the authors focus on two strategic tactics by plaintiffs' lawyers: the payment of mootness fees to plaintiffs' attorneys in meritless merger cases, and the filing of duplicative federal and state class actions made possible by the Supreme Court's Cyan *decision. They outline the policy objections to these practices and suggest that Congress should intervene to end them.*

By Gregory A. Markel and Sarah A. Fedner *

Despite judicial and congressional efforts to reduce and regulate meritless or unnecessary securities claims, the total number of securities cases increased dramatically in 2017 and that higher level of filings continued in 2018 and 2019. *See* Appendix 1. In 2019, there were 428 securities class actions filed in federal and state court, an unprecedented number since 2001.[1] This is almost double the average annual number filings from 1997-2018, which was 215.[2] Nearly one out of every 11 United States publicly traded companies faced a securities lawsuit in 2019.[3] The increase is largely driven by an upswing in merger claims over the last three years, which is attributable to a change in tactics by certain plaintiffs' attorneys as a result of the *Trulia* decision, as discussed below. The increase in overall filings is also partially attributable to more Securities Act of 1933 (the "1933 Act") claims being filed in merger cases and to a general increase in other (core) securities cases.[4]

Certain plaintiffs' attorneys are regularly developing new and creative ways to increase filings and circumvent unfavorable regulations or court rulings.[5] Two examples of these strategic practices emerged following the

[1] Cornerstone Research, *Securities Class Action Filings-2019 Year in Review* at 14 (2020), *available at* https://www.cornerstone.com/Publications/Reports/Securities-Class-Action-Filings-2019-Year-in-Review. *See also* Kevin M. La Croix, The D&O Diary, Cornerstone Research: Combined Federal and State Data Shows Securities Filings at "Record Levels" (2020), *available at* https://www.dandodiary.com/2020/01/articles/securities-litigation/cornerstone-research-combined-federal-and-state-data-shows-securities-filings-at-record-levels/.

[2] Cornerstone Research, *Securities Class Action Filings-2019 Year in Review* at 14.

[3] Kevin M. La Croix, The D&O Diary, Federal Court Securities Suit Filings Remain at Elevated Levels (2020), *available at*

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https://www.dandodiary.com/2020/01/articles/securities-litigation/federal-court-securities-suit-filings-remain-at-elevated-levels/.

[4] Appendix 1. *See also* La Croix, Federal Court Securities Suit Filings Remain at Elevated Levels.

[5] A small number of plaintiffs' firms is responsible for a large part of the increase in the questionable merger claims. The majority of plaintiff class action law firms are not engaged in bringing abusive merger claims.

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INSIDE THIS ISSUE

Delaware Court of Chancery's decision in the *Trulia* case[6] and the Supreme Court's decision in the *Cyan* case.[7] In the aftermath of these two rulings, plaintiffs moved to jurisdictions with more favorable rules to pursue litigation that is detrimental to corporations, their shareholders, director and officer ("D&O") insurers, and wasteful of judicial system resources as a whole. As a result of these frequently meritless claims, defendants are now: (1) paying legal fees to plaintiff's attorneys for non-meritorious merger class actions through "mootness fees" and (2) facing concurrent securities class actions in multiple jurisdictions stemming from initial public offerings ("IPOs"), secondary offerings, and stock issued in mergers. As discussed below, regulatory reform is required to prevent continued abuses from mootness fees and the confusion and overlapping claims arising in the wake of *Cyan*, and the detrimental impact to corporations and insurers, which ultimately impacts their shareholders and customers. These practices are a privately imposed tax on the United States' economy, which only benefits a small, but determined segment of plaintiffs' firms.

I. MOOTNESS FEES

The Delaware Court of Chancery's 2016 decision in *In re Trulia, Inc. Stockholder Litigation* led to a new trend in merger litigation. Certain plaintiffs' firms flocked to federal court and filed cases without hopes of meaningful corrective disclosures or recovery, but with the sole intent of obtaining attorneys' fees in exchange for voluntary dismissals and non-material supplemental disclosures. These payments have commonly become known as mootness fees. This practice raises serious policy concerns surrounding frivolous securities litigation, which likely can only be remediated completely through congressional reform of securities law.

A. Background

Beginning in 2009, filings of class action claims challenging mergers increased substantially. These cases generally challenged the sufficiency of shareholder disclosures or the overall fairness of the deals. As of 2015, the year before the *Trulia* decision, roughly 95% of merger transactions valued at more than $100 million were challenged.[8] 60% of these challenges were filed in Delaware courts, and more often than not in Chancery Court, while only 19% were filed in federal courts in other states.[9]

These cases were normally resolved in early settlements with corrective disclosures, which provided very broad releases of future class claims for defendants and, like most settlements, were often approved by the courts. Because these corrective disclosures theoretically benefitted shareholder members of a class, plaintiffs' attorneys were also generally awarded attorneys' fees by the courts under the common law corporate benefit doctrine. The disclosures supposedly provided shareholders with information material to making an informed decision. In reality, however, as the volume of cases increased, the added disclosure they provided became much less meaningful and really a makeweight of no value to justify plaintiffs' counsels' attorney fees. In many cases, the corrective disclosures were nearly pointless and did not change shareholder votes. Thus, many class actions seeking supplemental disclosures became a vehicle for plaintiffs' firms to obtain attorneys' fees for little, if any, meaningful benefit for shareholders. Since class actions were created to benefit a class of injured claimants, there was a fairly obvious disconnect between the theoretical purpose and the reality of the motive behind many merger cases that were seeking only largely unnecessary additional disclosures and attorneys' fees.

[6] *In re Trulia, Inc. Stockholder Litigation*, 129 A.3d 884 (Del.Ch. 2016).

[7] *Cyan v. Beaver County Employees Retirement Fund*, 138 S.Ct. 1061 (2018).

[8] Matthew D. Cain, Jill E. Fisch, Steven Davidoff Solomon, & Randall S. Thomas, Mootness Fees, 72 Vand. L. Rev. 1777, 1785 (2019).

[9] *Id.*

B. The Trulia *Decision*

The Delaware Chancery's Court decision in *Trulia* sought to put an end to this practice by limiting disclosure-only settlements to those that resulted in disclosures that added significant value to class members and provided releases of sensible scope. In that case, the court refused to approve a proposed settlement, which included supplemental disclosures and attorneys' fees in exchange for a broad release, finding that the proposed disclosure was not "plainly material" as defined under Delaware law.[10] The court cautioned that, unless there was "a substantial likelihood that the disclosure of the omitted fact would have been viewed by the reasonable investor as having significantly altered the `total mix' of information made available,"[11] proposed disclosure-only settlements and accompanying attorney's fees would not be approved going forward by the Chancery Court.[12]

*C. Federal Merger Litigation Post-*Trulia

Trulia came as the culmination of several then recent Delaware Chancery Court decisions and it made clear there was a new regime in Delaware Chancery Court for settlements of merger cases. However, *Trulia* did not apply in other forums. Certain plaintiffs' firms took advantage of this by challenging mergers in alternative jurisdictions. In 2016, the rate of merger litigation plummeted in Delaware state court by almost 50% and continued to decrease in the years thereafter.[13] This trend was accompanied by an immediate uptick in merger litigation in federal courts.[14] In 2017, 198 merger-objection lawsuits were filed in federal court, 182 were filed in 2018, and 160 were filed in 2019.[15] These numbers reflect a staggering increase compared to the 34 merger-objection lawsuits filed in federal court in 2015, the year prior to *Trulia*.[16] As of 2018, only 5% of completed deals were challenged in Delaware Chancery Court, while 92% were challenged in federal court.[17] This evidence is clear that *Trulia* largely moved most merger claims out of Delaware Chancery Court.

Not only did the rate of filings increase in federal court, but the number of class action cases resolved through voluntary dismissals before a class was certified skyrocketed. Starting in 2016, in many merger cases, there was a voluntary dismissal by plaintiffs and a payment of attorneys' fees to plaintiffs. These mootness fees cases generally did not require court approval of settlements, and were characterized by non-material supplemental disclosures and payment of mootness fees. The agreements resolving these cases were generally made through party negotiations and received no court supervision. There was no court review, because settlements before class certification are generally treated as individual actions and generally do not require court approval. By 2018, 92% of these voluntary dismissals of merger cases resulted in the payment of mootness fees.[18]

Mootness fees are infrequently challenged. Because the cases to be resolved are voluntarily dismissed prior to class certification, notice to class members is not required. Defendants generally pay rather than challenge mootness fee demands, likely because they are trying to avoid delays in completing merger transactions and it is less costly to pay a mootness fee than fully litigate a case on the merits.

*D. Post-*Cyan *Decisions*

There has been little federal case law on mootness fees since the *Trulia* decision, given the lack of litigation on the merits and, by definition, they are paid in connection with cases dismissed before class

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[10] *Id.* at 898-99.

[11] *Id.* at 899.

[12] However, in an unpublished decision a few months later, the Delaware Chancery Court appeared to apply a different standard to mootness dismissals as opposed to court approval of proposed class settlements. The court distinguished the *Trulia* decision, stating:

> This Court in *Trulia* made clear that, to support a settlement and class-wide release based on disclosures only, the materiality of the disclosures to stockholders must be plain. The mootness context, in my view, supports a different analysis. That is because, here, the individual plaintiffs have surrendered only their own interests; the dismissal is to them only, not to the stockholder class.

In re Xoom Corp. Stockholder Litigation, No. 11263–VCG, WL 4146425, at *3 (Del.Ch. Aug. 4, 2016). The court upheld a $50,000 mootness fee award and noted "a fee can be awarded if the disclosure provides some benefit to stockholders, whether or not material to the vote. In other words, a helpful disclosure may support a fee award in this context." *Id.*

[13] *Cain, supra* note 8, 72 Vand. L. Rev. at 1781, 1788.

[14] The rate of merger challenges filed in state courts also increased, but the majority of filings occurred in federal court.

[15] Cornerstone Research, *Securities Class Action Filings-2019 Year in Review* at 14.

[16] *Id.*

[17] *Cain, supra* note 8, 72 Vand. L. Rev. at 1782.

[18] *Id.* at 1792-93.

certification. However, in two notable cases, federal courts followed the reasoning in *Trulia,* decrying the tawdriness and "racket" that characterizes too many merger case resolutions.

First, in a 2016 opinion by the highly respected Judge Richard Posner, the Seventh Circuit[19] cited to *Trulia* and held that proposed class action settlements and accompanying attorneys' fees should be rejected unless the supplemental disclosure is "plainly material." [20] The court referred to disclosure-only settlements as "no better than a racket" and noted "the oddity of this case is the absence of *any* indication that members of the class have an interest in challenging the reorganization. The only concrete interest suggested by this litigation is [plaintiffs' attorneys'] interest in [their] fees, which of course accrue solely to class counsel and not to any class members."[21] The Seventh Circuit reversed the district court's approval of the proposed class settlement and instructed the district court on remand to "give serious consideration to either appointing new class counsel . . . or dismissing the suit."[22] Ultimately, the case was voluntarily dismissed by plaintiffs without any payment of fees.[23]

Unfortunately, this "plainly material" rule has not been uniformly followed in federal and state courts outside of Delaware in cases of disclosure-only settlements. Importantly, in most cases, the *Trulia* rule has not been applied to mootness fees in voluntary dismissals prior to class certification that generally do not even come to the court's attention.

However, in a tiny number of cases, courts have addressed mootness fees. In an unusual case from the Northern District of Illinois, a shareholder sought to intervene and object to a settlement stipulation, which disclosed the payment of mootness fees prior to class certification.[24] Citing, inter alia, *Trulia* and Posner, the court found that the supplemental disclosures were not "plainly material" and used its "inherent authority" to abrogate the settlement agreement and order the return of any mootness payments. The court emphasized the inherent problems with this practice, stating:

> plaintiffs' attorneys were rewarded for suggesting immaterial changes to the proxy statement. [Defendant] paid plaintiffs' attorney's fees to avoid the nuisance of ultimately frivolous lawsuits disrupting the transaction with Frensenius. The settlements provided [Defendant's] shareholders nothing of value, and instead caused the company in which they hold an interest to lose money. The quick settlements obviously took place in an effort to avoid the judicial review this decision imposes. This is the "racket" . . . which stands the purpose of Rule 23's class mechanism on its head; this sharp practice "must end."[25]

The settlement agreements were abrogated by the court and plaintiffs' counsel was ordered to return any attorney's fees they had received.[26]

This decision is unusual because it is quite rare for a court to be made aware of mootness payments, let alone the opportunity to consider whether a settlement with mootness fees and voluntary dismissal prior to class certification is appropriate. It is also unusual because mootness fees are generally not disclosed and, therefore, shareholders do not have notice or the opportunity to intervene or object.

E. Policy Concerns Relating to Mootness Fees

There are many significant policy concerns regarding the effect of unregulated mootness fees on the integrity of our judicial system. Certain plaintiffs' firms are filing these suits with increasing regularity in what is akin to a tax on mergers that (1) does not provide any benefit to the shareholders of corporations; but (2) is costly for the corporation and the shareholders the lawsuit is purportedly designed to benefit; and (3) is detrimental to the economy. Some of the policy concerns are outlined below:

1. *Frivolous Litigation*: There is strong evidence suggesting that many of these cases are filed solely to recover attorneys' fees for plaintiffs' counsel and

[19] This case made its way to the Seventh Circuit after a shareholder appealed the Northern District of Illinois' approval of the proposed class action settlement.

[20] 832 F.3d 718, 725-26 (2016).

[21] *Id.* (emphasis in original).

[22] *Id.*at 726.

[23] 1:14-cv-09786, Dkt. No. 112 (N.D. Ill. Dec. 13, 2016).

[24] 385 F. Supp. 3d 616, 619, 623 (N.D. Ill. 2019).

[25] *Id.* at 623.

[26] *Id.* Plaintiffs appealed this decision, challenging a shareholder's ability to intervene and object to mootness fees. *See* No. 19-2408, Dkt. No. 20 (7th Cir. Oct. 18, 2019). Oral argument is scheduled in the Seventh Circuit for April 2020. *Id.* at Dkt. No. 55.

lack any merit. First, the cases have generally been filed by a handful of plaintiffs' firms who, historically, had not actively litigated or obtained meaningful awards/settlements in merger litigation.[27] These frequent-filer firms went through the normal settlement approval process for class actions in less than 5% of their cases, suggesting that the cases were likely filed only in an effort to obtain mootness fees.[28] These firms also repeatedly used many of the same named plaintiffs to file cases.[29] In addition, post-*Trulia*, filings in Delaware Chancery Court became scarce despite the fact that it is still a viable venue for stockholder claims. Finally, these cases are rarely litigated on the merits and most of the time there is no assessment of whether the complaints state a claim.

2. *No Benefit to Shareholders*: Corrective disclosures were theoretically intended to provide shareholders with necessary information to make informed investment decisions. However, without applying a "plainly material" standard to supplemental disclosures, shareholders are unlikely to gain little if any benefit from such disclosures. In most cases, supplemental disclosures have not impacted shareholder votes and the cases seeking mootness fees are not pursued to uphold any other shareholder rights. By wasting a corporations' funds fighting a meritless lawsuit, these lawsuits actually harm the shareholders they were supposedly designed to protect when the cases were filed.

3. *Lack of Court Oversight*: These litigations are generally resolved through private negotiations between the parties prior to the class certification stage and, therefore, courts are not required to approve any mootness fees. Nor are courts required to evaluate the merits of the claims at issue to assess the fairness of the settlement terms to the class. Except in unusual circumstances, these cases are not in a procedural posture for the courts to address the provision for attorneys' fees.

4. *Lack of Transparency*: There is a general lack of transparency regarding whether mootness fess are paid at all and the amount of such payments. Because such cases are voluntarily resolved prior to class certification, shareholders generally do not receive notifications. Most court filings are devoid of any mention of mootness fees, although some may be disclosed in a press release or SEC filing. However, because there is no disclosure requirement, it is unclear how many cases culminate in mootness fees and the amount of such fees. Extraction of these fees is, in most cases, not in shareholders' interests.

5. *Illegitimate Tax on Corporations*: Corporations are paying a fairly hefty price because of mootness resolutions. One study found that the median mootness fee from 2014 to 2017 ranged from $200,000-$450,000.[30] In 2017, mootness fees averaged approximately $265,000 per case and totaled approximately $2.32 million.[31] There is evidence that the average may have declined recently.[32] The overall cost could also be much larger in some cases since there is no requirement that mootness fees be disclosed and parties usually do not do so in court filings. Moreover, these numbers do not take into account the additional expense to defendant corporations that also pay fees for defense costs. Companies have had to pay increasing attorneys' fees to defend themselves in these actions as the mootness fee phenomenon spreads.

6. *Avoidance of the Private Securities Litigation Reform Act* (*"PSLRA*"): As noted in an article by Fordham Professor Sean J. Griffith, plaintiffs may also be able to escape several PSLRA mandates through mootness resolution.[33] Notably, the PSLRA's requirement that attorneys' fees cannot exceed a "reasonable percentage" of any damages or prejudgment interest awarded by the court does not apply to mootness fees, which are negotiated without any court involvement. Plaintiffs are also able to avoid the PSLRA's prohibition on a plaintiff leading more than five class actions within three years by their voluntarily dismissing their claims prior to class certification.[34] Thus, the PSLRA's intent to do away with serial filing plaintiffs can be and is being thwarted. Finally, because these cases

[27] Griffith, *Class Action Nuisance Suits: Evidence from Frequent Filer Shareholder Plaintiffs*, Cambridge International Handbook of Class Actions at 12-13 (2020); *Cain*, *supra* note 8, 72 Vand. L. Rev. at 1797-99.

[28] *Cain*, *id*.

[29] Griffith, *supra* note 28 at 12-13.

[30] *Cain*, *supra* note 8, 72 Vand. L. Rev. at 1803.

[31] *Id.* at 1804-05.

[32] *Id.* at 1803.

[33] Griffith, *supra* note 28.

[34] 15 U.S. Code § 78u-4(b)(1).

are voluntarily dismissed before any motion to dismiss or final adjudication on the merits, there are no Rule 11 findings or assessment of whether plaintiffs pled each alleged misstatement or omission with specificity and in good faith.[35]

F. Proposed Regulatory Reform

Several changes should be made to federal laws in order to discourage mootness fee resolutions. First, amendments should be made to the Federal Rules of Civil Procedure ("FRCP") and/or the PSLRA requiring court approval of voluntary dismissals of purported securities class actions. Second, the FRCP and/or the PSLRA should be amended to require disclosure of mootness payments to all potential class members prior to a court hearing on such dismissals to allow the courts and shareholders an opportunity to intervene and object to the fees. Plaintiffs could attempt to avoid any such new requirements by filing individual actions instead. However individual actions may not generate much in the way of mootness fees.[36] Finally, the FRCP and/or the PSLRA should be amended to prohibit the payment of mootness fees unless the proposed supplemental disclosure is "plainly material."[37]

II. *CYAN* SPAWNS DUPLICATIVE STATE AND FEDERAL LITIGATION

A 2018 Supreme Court decision has also caused the migration of securities suits to new forums. Following the Supreme Court's ruling in *Cyan*, plaintiffs firms began filing securities class actions pursuant to the 1933 Act in state court with increasing regularity. The *Cyan* ruling allows plaintiffs to avoid at least some aspect of the PSLRA's provisions designed to eliminate meritless securities litigation by filing 1933 Act claims in state court while simultaneously filing nearly identical actions in federal court.[38] Although the *Cyan* decision was based upon statutory interpretation, the consequences of the decision can and do result in duplicative, unnecessary, unfair and costly litigation. Textual amendments to the Securities Litigation Uniform Standards Act ("SLUSA") or the 1933 Act are required to eliminate a loophole in the law and those who take advantage of it.

A. Background

In 1995, Congress enacted the PSLRA in an effort to reform securities litigation. After its enactment, many plaintiffs brought cases to state court to avoid the PSLRA's procedural protections. In 1998, Congress responded by enacting SLUSA, which, among other things, amended jurisdictional provisions to deprive state courts of concurrent jurisdiction over certain securities class action claims and permitted the removal of certain types of securities class actions to federal court.

However, Section 22(a) of the 1933 Act included provisions, which specifically: (1) gave state courts concurrent jurisdiction over claims brought under the 1933 Act and (2) prohibited the removal of such claims, originally brought in state court, to federal court. After SLUSA's enactment, a circuit court split developed regarding whether SLUSA had superseded these provisions.

B. The Cyan *Decision*

The split in circuits was ultimately resolved in the Supreme Court's unanimous decision in *Cyan v. Beaver County Employees Retirement Fund*.[39] In that case, shareholders brought a securities class action exclusively under the 1933 Act against telecommunications company Cyan, Inc. in California state court. Cyan moved for judgment on the pleadings, arguing that the SLUSA amendment eliminated state court jurisdiction over such claims. Plaintiffs opposed and asserted that SLUSA only intended to deprive state courts jurisdiction over securities class actions brought under state law, not class actions brought under the 1933 Act. The California Superior Court denied Cyan's motion and the state appellate courts denied review of the trial court decision. The Supreme Court granted Cyan's petition for certiorari to answer the question of whether SLUSA's amendment deprived state courts of jurisdiction over class action claims brought exclusively under the 1933 Act.

The Supreme Court affirmed the decision below and held: (1) SLUSA did not deprive state courts jurisdiction over cases brought solely under the 1933 Act and

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[35] *Id*. § 78u-4(a)(2)(A).

[36] *Cain*, 72 Vand. L. Rev. at 1812 n.127.

[37] Because changing laws or regulations can be a drawn out process, commentator and Fordham Professor Sean J. Griffith, has also suggested that corporations amend their by-laws to include no-pay provisions for attorneys' fees or that D&O insurers enter into some sort of incentive agreement to encourage defendants to challenge the practice on the merits. *See* Dean Seal, Law360, *Fordham Professor Urges Insurers To Fight 'Mootness Fees', available at*: https://www.law360.com/articles/1238984.

[38] These concurrent litigations are usually filed by different plaintiffs.

[39] 138 S.Ct. 1061 (2018).

(2) SLUSA does not authorize removal of such claims to federal court.[40] The Supreme Court based its decision upon its close reading of SLUSA's text and rejected Cyan's arguments that the legislative purpose and history of SLUSA was to prevent plaintiffs from avoiding the PSLRA's procedural protections by filing securities claims in state court.

C. The Aftermath of Cyan

As anticipated, the number of 1933 Act claims filed in state court increased immediately following the *Cyan* decision. 32 claims under the 1933 Act were filed in state court in 2018.[41] This increased by 40% in 2019, with 49 state court cases being filed.[42] As of 2019, the number of 1933 Act cases brought in state court exceeded those brought in federal court, with the majority of claims being brought in New York and California state courts.[43]

Nearly half of the state court cases filed in 2018-2019 also had concurrent federal litigation filed.[44] In the eight years prior to the *Cyan* decision, only four companies faced concurrent 1933 Act litigation.[45] In the less than two years following *Cyan*, seven companies have faced concurrent 1933 Act litigation, including one company facing simultaneous litigation in five separate jurisdictions.[46]

Several cases filed or resolved after the *Cyan* decision serve as good examples of the confusion and uncertainty arising from the ruling. For example, state courts have reached conflicting decisions regarding whether federal safeguards, such as some of those provided by the PSLRA and federal common law principles, apply in state court proceedings. In two New York County Supreme Court decisions, Justice Saliann Scarpulla held that the PSLRA's stay of discovery during a pending motion to dismiss did not apply in state court proceedings and that to hold otherwise would "undermine *Cyan's* holding."[47] Yet, a subsequent New York decision held the opposite, stating that *Cyan* did not control whether the PSLRA discovery stay applied to state courts and "the simple, plain, and unambiguous language expressly provides that discovery is stayed during a pending motion to dismiss '[i]n any private action arising under this subchapter.'"[48] Trial courts in other states have reached conflicting decisions on this issue,[49] and the New York appellate courts have yet to weigh in.

Another state court decision in New York raises interesting questions regarding whether federal common law pleading standards apply to 1933 Act litigation in state court. In *In Re Net Shoes Securities Litigation*,[50] Justice Andrew Borrok dismissed claims brought under the 1933 Act, alleging false and misleading statements, by expressly applying federal case law regarding opinion statements, puffery, and the bespeaks caution doctrine. It is unclear whether other state courts will follow suit.

Finally, a recent decision[51] suggests that *Cyan* applies equally to 1933 Act claims based not only upon initial public offerings, but also secondary public offerings. In that case, noting the pendency of the Supreme Court's decision in *Cyan*, the Eastern District of Pennsylvania denied defendants' request to remove a state court case, which alleged defendants violated the 1933 Act in connection with a secondary offering. The case was ultimately resolved through a $50 million settlement in the Pennsylvania Chester County Court of Common Pleas. Thus, defendants face the risk of multiple, concurrent litigations in the context of both initial and secondary securities offerings, and even with respect to securities issued in merger transactions.

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[40] *Id*. at 1064-65.

[41] Cornerstone Research, *Securities Class Action Filings-2019 Year in Review* at 4, 19.

[42] *Id.*

[43] *Id.*

[44] *Id.*

[45] *Id.* at 24.

[46] *Id.*

[47] *In re Dentsply Sirona, Inc. v. XXX*, Index No. 155393/2018, 2019 WL 3526142 (Sup. Ct. N.Y. Cnty. Aug. 2, 2019); *See also In re PPDAI Group Securities Litigation*, No. 654482/2018, 2019 WL 2751278 (Sup. Ct. N.Y. Cnty. July 1, 2019).

[48] *In re Everquote, Inc. Securities Litigation*, Index No. 651177/2019, 2019 WL 3686065 (Sup. Ct. N.Y. Cnty. Aug. 7, 2019) (Borrok, J.).

[49] *Switzer v. Hambrecht & Co*., No. CGC-18-564904, 2018 WL 4704776, at *1 (Cal. Super. Ct. Sept. 19, 2018) (holding the PSLRA's discovery stay does not apply in state court); *cf. City of Livonia Retiree Health and Disability Benefits Plan v. Pitney Bowes*, No. X08-FST-CV-18-6038160-S, 2019 WL 2293924 at *4 (Conn. Super. Ct. May 15, 2019) (holding the PSLRA discovery stay applies).

[50] 157435/2018, 2019 N.Y. Slip Op. 29219 (Sup. Ct. N.Y. Cnty. July 16, 2019).

[51] Civ. No. 17-1466, Dkt. No. 47 (E.D. Pa. Aug. 28, 2017).

D. Policy Concerns

Like the *Trulia* decision, *Cyan* raises significant policy concerns, including the overall undue burden on companies seeking to go public or engage in secondary offerings. These include:

1. *Avoidance of the PSLRA*: The Supreme Court in the *Cyan* decision itself acknowledged that plaintiffs can avoid at least some of the procedural protections of the PSLRA by filing 1933 Act claims in state court. Indeed, whether the automatic stay of discovery under the PSLRA is applicable in state court has resulted in inconsistent decisions. While the applicability of some provisions of the PSLRA is still in doubt in state court, it is clear that plaintiffs can avoid the pleading requirements of the PSLRA by filing in state court. Thus, plaintiffs can now pursue cases that would otherwise be dismissed or deemed non-meritorious under the PSLRA in federal court. This undermines the very purpose of congress' enactment of regulations such as SLUSA and the PSLRA, which required, not only that plaintiffs state a fraud claim with particularity as under FRCP Rule 9(b), but also applies a very high standard of particularity for pleading scienter, which Rule 9(b) does not.

2. *Concurrent Litigation*: In the wake of the *Cyan* decision, companies have been forced to defend themselves in an increasing number of multi-front litigations in multiple jurisdictions. Companies seeking to go public now face the risk of litigation in federal and state or multiple state courts.

3. *Conflicting Obligations*: Concurrent litigation in state and federal courts could result in conflicting decisions. This is especially true since the procedural safeguards applicable to securities cases in federal court may not apply in state court.

4. *Waste of Judicial Resources*: Permitting claims to be brought in multiple jurisdictions at the same time is a waste of the resources and time of courts in those jurisdictions. Concurrent litigation delays complicates the resolution of such claims and places an unnecessary strain on judges, litigants, attorneys, D&O insurers, and potentially, jurors. While courts could stay one of the cases, that leaves for courts ad hoc decisions on whether to stay and the results have not been uniform.[52]

5. *Lack of State Court Familiarity*: Because federal court is the designated forum for many claims arising under the securities laws, many state courts are less familiar with these claims than many federal courts. This unfamiliarity, coupled with the lack of PSLRA protections, has and likely will continue to result in lower dismissal rates of non-meritorious claims that would have been dismissed in an identical federal suit. arising under the securities laws, many state courts are less familiar with these claims than many federal courts. This unfamiliarity, coupled with the lack of PSLRA protections, has and likely will continue to result in lower dismissal rates of non-meritorious claims that would have been dismissed in an identical federal suit.

6. *Difficulty Determining Class Damages*: Section 11 provides a generally accepted methodology for calculating damages in securities class actions brought under the 1933 Act, which has been complicated by the *Cyan* decision. Estimating damages early in a case could well be more difficult due to differing class definitions in the overlapping cases, differing shares outstanding at the time of the filings, a lack of uniformity in pleading requirements for negative causation,[53] and overlapping estimations of alleged artificial inflation in the stock price.[54] The added complexity of duplicative cases may complicate settlement negotiations for plaintiffs and defendants.

7. *Corporate Tax*: All of the aforementioned issues, ultimately result in an unjustifiable tax on corporate resources. Companies seeking to go public or obtain a secondary offering now face the cost of defending themselves in multiple jurisdictions. This risk also leads to increased insurance premiums for IPO companies or secondary offerings, as well as higher retentions of liability for insureds. This is

[52] Michael Klausner, Jason Hegland, Carin LeVine, and Jessica Shin, Stanford Securities Special Report for D&O Symposium,

footnote continued from previous column…

State Section 11 Litigation in the Post-Cyan Environment — An Update at 26 (2020).

[53] Negative causation is an affirmative defense set forth under Section 11 whereby defendants can argue the depreciation in plaintiffs' stock was caused by factors other than defendants' alleged misstatements or omissions.

[54] Nessim Mezrahi, The D&O Diary, *Guest Post: Time to Resolve Post-Cyan Securities Class Action Confusion* (2019), *available at* https://www.dandodiary.com/2019/08/articles/securities-litigation/guest-post-time-to-resolve-post-cyan-securities-class-action-confusion/.

detrimental to the overall well-being of companies, their shareholders, and the economy.

D. Proposed Regulatory Reform

The *Cyan* decision was based upon a reading of the 1933 Act's and SLUSA's texts. Thus, a modification of one or both statutes is required to remedy all of the negative consequences resulting from the decision. In the authors' view, Congress should amend the language of SLUSA and the 1933 Act to explicitly designate federal court as the sole jurisdiction for all claims brought under the 1933 Act.

Because regulatory change can be slow, companies should strongly consider amending their by-laws or certificates of incorporation in the interim to designate federal court as the exclusive jurisdiction for all shareholder claims arising under the 1933 Act. The enforceability of these provisions was recently upheld by the Delaware Supreme Court..[55] In March 2020, the court held that provisions designating federal court as the exclusive jurisdiction for such claims were valid under Delaware law, specifically stating "Delaware courts attempt 'to achieve judicial economy and avoid duplicative efforts among courts in resolving disputes.'[Federal forum selection clauses] advance these goals."[56] If Delaware companies add the suggested forum selection clause to their by-laws or certificate they will likely avoid the adverse effects of *Cyan* described above. If other courts adopt the Delaware Supreme Court's position the problems created by *Cyan* will be well on their way to being solved.

III. CONCLUSION

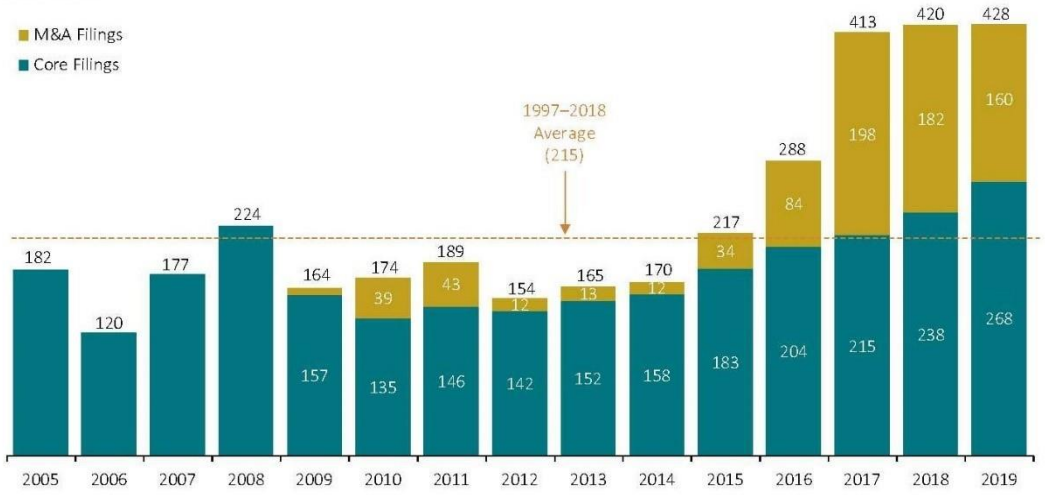
As exemplified by the statistics on securities class actions post-*Cyan* and *Trulia*, corporations, their shareholders and insurers face abusive securities litigation practices and a situation where long-standing statutes are having unwanted consequences that undermine the clear intent of securities laws adopted by Congress, judicial opinions, and overall judicial fairness principles. These practices are raising the cost of doing business for corporations, D&O insurance companies, and their policy holders. This negative impact on the well-being of a corporation can trickle down to shareholders, who are theoretically the ones who in these suits are supposed to benefit. Congress should intervene and amend the relevant statutes to eliminate these problems. In the case of *Cyan* and its aftermath, the problems could be largely cured by the adoption of bylaws by the companies and the new Delaware rule by other courts.■

[55] *Salzburg v. Sciabacucch*i, C.A. No. 2017-0931-JTL, (Del. March 18, 2020).

[56] *Id*. at 52.

Appendix

Figure 4: Class Action Filings Index® (CAF Index®) Annual Number of Class Action Filings 2005–2019



Note: This figure begins including state 1933 Act filings in the annual counts in 2010. Parallel class actions are only reflected as a single filing.

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