Skadden

Securities Class Action Filings Continue Record Pace

Partners

Jay B. Kasner / New York

Scott D. Musoff / New York

Susan L. Saltzstein / New York

Several securities litigation trends over recent years show no signs of abating in 2020. Federal securities class action filings seem likely to remain at elevated levels. Last year, for the third consecutive year, more than 400 securities class actions were filed in federal court. Given the high volume of filings and the fact that the number of publicly listed companies has decreased by nearly two-thirds since 2000, the chance of a public company being named in a securities class action has grown exponentially.

Although filings in 2019 reflected a moderate drop in the number of federal merger objection suits, this decline was offset by an increase in more traditional class action cases — *i.e.*, those seeking relief under Section 10(b) of the Securities Exchange Act of 1934 or Section 11 of the Securities Act of 1933. These statistics also do not account for the increased number of Securities Act suits filed in state court due to the Supreme Court's decision in *Cyan Inc. v. Beaver County Employees Retirement Fund*, which held that Securities Act cases were not removable to federal court. Technology and health care/life sciences companies continued to be targeted as a result of their more volatile stock price performance, a trait unlikely to change in 2020.

Against this backdrop, the impact of several recently decided cases and one pending U.S. Supreme Court case will become clearer in 2020. Companies should understand the potential impact these and other trends are likely to have on the securities litigation landscape.

Event-Driven Cases Are Likely To Remain a Focus

We expect plaintiffs firms will continue to gravitate toward so-called event-driven litigations — cases where the catalyst is the disclosure or occurrence of a significant event. These triggering events tend to reflect general risks that cut across multiple industries, such as data breaches or other cybersecurity incidents; environmental accidents; natural disasters; allegations of sexual harassment; and alleged regulatory violations, such as those arising under the Foreign Corrupt Practices Act. With numerous cases at the pleading stage, we may soon get more insight into how likely event-driven lawsuits are to survive motions to dismiss and thus gain traction at the district court level.

This decisional law, as it develops, will shed light on the viability of different allegations and theories of recovery. One typical pleading tactic, for example, is to claim on the heels of an alleged regulatory violation that the company misled investors regarding its compliance with an internal code of conduct or governing law. For instance, the U.S. Court of Appeals for the Second Circuit in *Singh v. Cigna Corp.* affirmed the lower court's dismissal of a putative class action, holding that alleged violations of generic statements included in Cigna's code of ethics could not support a claim for alleged securities fraud. The *Cigna* decision, however, did not prevent claims from moving forward against Signet Jewelers Ltd., where, following public reports of alleged sexual harassment, the plaintiffs alleged that the company violated its internal corporate policies prohibiting such behavior. Taken together, these cases suggest that courts will not hesitate to dismiss claims premised on vague or generic corporate statements but will permit them to move forward if plaintiffs provide strong and detailed factual allegations.

This article is from Skadden's *2020 Insights*.

This memorandum is provided by Skadden, Arps, Slate, Meagher & Flom LLP and its affiliates for educational and informational purposes only and is not intended and should not be construed as legal advice. This memorandum is considered advertising under applicable state laws.

Four Times Square
New York, NY 10036
212.735.3000

Supreme Court Decision in *Cyan* Will Continue To Shape Securities Litigation

The U.S. Supreme Court's 2018 decision in *Cyan* is expected to continue to impact Securities Act litigation, as plaintiffs' firms have increased the number of Securities Act filings in both federal and state courts, requiring the courts to wrestle with several thorny issues relating to stays, transfer and coordination. In *Cyan*, the Supreme Court held that the Securities Litigation Uniform Standards Act of 1998 did not authorize federal courts to remove cases brought solely under the Securities Act, and that state courts may exercise jurisdiction over such cases.

In the immediate aftermath of the ruling, we predicted that plaintiffs' firms, emboldened by the decision, would file cases in state courts with greater frequency — including in jurisdictions, such as New York, that previously refused to hear these suits. (See "Supreme Court Holds That Class Actions Brought Under Securities Act in State Court Are Not Removable.") Last year, more Section 11 cases were filed in state court than in 2018, with a substantial number landing in New York state court. According to data compiled by the Professional Liability Underwriting Society, more than 75% of these post-*Cyan* suits were filed in state court alone or in both state and federal court. Conversely, less than 25% of Section 11 cases were filed in federal court alone. By way of comparison, in the three years before *Cyan* — roughly seven out of every 10 Section 11 cases (or 67%) were brought in federal court on a stand-alone basis, making it possible for defense counsel to consolidate or coordinate parallel filings through the Judicial Panel on Multidistrict Litigation, motions to transfer or otherwise.

The post-*Cyan* migration of cases to state court, by contrast, has complicated case management efforts. For example, in 2019, nearly half (48%) of all new Securities Act matters included parallel state and federal filings (as compared to 16% in the three years before *Cyan*). Because no procedural mechanism exists for consolidating — or even coordinating — these overlapping suits, corporate defendants have been forced to seek discretionary stays and other alternative forms of relief. These efforts have led to several inconsistent rulings at the state court level. For instance, on two occasions in 2019, the Commercial Division of the New York Supreme Court denied a stay even though the federal cases included Exchange Act claims that could only have been brought in federal court. In contrast, at least one Massachusetts state court, several in California and even one New York court granted stays in favor of federal cases. One factor that appears to have favored stays is whether the federal case was filed first. State courts also have disagreed as to whether the automatic discovery stay provisions of the Private Securities Litigation Reform Act of 1995 apply to Securities Act claims brought in state court.

As these examples suggest, the law surrounding Cyan remains unsettled. With multiple Securities Act cases pending in New York, California and elsewhere, the new year may provide more clarity as to how state courts are resolving these procedural issues. Equally important, we hope to learn more in 2020 about how different state courts are applying the substantive elements of Securities Act claims at the motion to dismiss stage. In 2019, defendants won several important victories in this regard. Rulings this year may provide more insight into whether trends are developing within or among states.

Supreme Court May Address Whether Plaintiffs Can Use ERISA Stock-Drop Suits To Plead Around the Securities Laws

In *Retirement Plans Committee of IBM v. Jander*, the U.S. Supreme Court remanded to the Second Circuit a closely watched case regarding whether plaintiffs can effectively use ERISA to plead around the federal securities laws. In *Jander*, the plaintiffs accused plan administrators, all of whom were company insiders, of violating ERISA by failing to disclose allegedly negative information about IBM's microelectronics business. The plaintiffs claimed that during the relevant time period, plan administrators should have understood that the disclosure of this nonpublic information (along with a corresponding drop in the price of IBM stock) was inevitable. As a result, the plaintiffs alleged, any prudent fiduciary would have concluded that silence — that is, waiting to reveal the adverse information — would do more harm than good. In reversing the dismissal of the plaintiffs' complaint, the Second Circuit largely agreed with this framing of the "more harm than good" standard first enunciated by the Supreme Court in *Fifth Third Bancorp v. Dudenhoeffer*.

Before the Supreme Court, the IBM fiduciaries argued, in a position supported by the U.S. solicitor general, that when ERISA fiduciaries learn of inside information that may negatively affect the company's stock price, courts must evaluate a duty to disclose that information by looking solely to the federal securities laws. Reasoning from this premise, IBM has claimed that the Second Circuit's "inevitable disclosure" standard sweeps far more broadly — and is appreciably more lenient from a pleading perspective — than *Dudenhoeffer* permits. Indeed, IBM argued that the Second Circuit's test could, in some cases, require disclosure in situations where the federal securities laws do not. (See "2019-20 Supreme Court Update.")

The Supreme Court's decision leaves the issue unsettled as the case goes back to the Second Circuit for further proceedings because petitioners and the federal government had focused on the consistency between the securities laws and ERISA, arguments the Second Circuit never had

the chance to address. (See "Supreme Court Declines To Rule on ERISA Breach of Fiduciary Duty Pleading Standard for ESOP Cases.")

Other Issues To Look for in 2020

District and appellate courts likely will have an opportunity to consider two of the Supreme Court's more notable securities rulings from 2019: *Lorenzo v. SEC* and *Emulex Corp. v. Varjabedian*. In *Lorenzo*, the Court held that Francis Lorenzo, an investment banker, was liable under Subsections (a) and (b) of Rule 10b-5 for emailing clients a false and misleading investment solicitation that had been prepared by Mr. Lorenzo's boss. The Court's decision meant, in practical terms, that Mr. Lorenzo could be held responsible as a primary violator of Section 10(b) despite not having "made" the underlying statement. In 2020, *Lorenzo* may lead to an increase in private securities claims against disseminators who themselves did not make false and misleading statements, based on the theory that these defendants participated in a scheme to defraud investors.

We also will be tracking any fallout from *Emulex Corp. vs. Varjabedian*, a merger objection suit that was dismissed by the Court after oral argument and, crucially, before any decision was issued. The complaint had asserted violations of Section 14(e) of the Exchange Act, a provision that is routinely invoked by private plaintiffs in challenging the accuracy of tender offer materials. However, this long-recognized private right of action, may be in jeopardy: During oral argument, several justices questioned whether it was even appropriate for a private plaintiff to proceed under Section 14(e). Taking their cues from the Supreme Court, defendants in Section 14(e) suits are likely to challenge the very right of private investors to sue under this section of the Exchange Act. If one of these cases survives long enough, it may well serve as a vehicle for the Court to revisit whether a private right of action exists under Section 14(e).

This year will mark the 25th anniversary of the enactment of the Private Securities Litigation Reform Act of 1995, which was intended to curtail securities class action filings. Despite those intentions, we anticipate another year of record or near-record filing levels and will be closely watching a number of potential decisions that will continue to shape the securities litigation landscape.