Key Takeaways

Skadden

13th Annual Securities Litigation and Regulatory Enforcement Update

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On December 8, 2020, Skadden held the fourth and final installment of its annual Securities Litigation and Regulatory Enforcement Update, "Developments and Trends in Securities Litigation: A Year-End Update for 2020 and a Look Ahead to 2021." The virtual panelists were **Jay B. Kasner** and **Susan L. Saltzstein**, head and co-deputy head of Skadden's nationwide Securities Litigation Group; **Peter B. Morrison**, co-head of Skadden West Coast litigation practice; **Charles F. Smith**, head of Skadden's litigation and regulatory enforcement practice in Chicago; **Carol V. Gilden**, securities litigation partner at Cohen Milstein; and **Jack Flug**, managing director at Marsh & McLennan.

The webinar focused on several important developments in securities litigation from 2020 and the panelists' predictions on how trends will change or continue in 2021. Among other topics, the panelists discussed (i) securities litigation filing and settlement trends, including the recent upswing in cases involving special purpose acquisition companies (SPACs); (ii) the potential impact of recently appointed Justice Amy Coney Barrett on the U.S. Supreme Court's securities litigation jurisprudence; (iii) lower court interpretations of several recent Supreme Court decisions, including *Lorenzo*, *Omnicare*, *Cyan* and *Jander*; and (iv) developments in the Ninth Circuit.

Below are high-level takeaways on each topic.

Securities Filings Remain Elevated Despite the Pandemic

Despite unprecedented disruptions to the court system from the COVID-19 pandemic, plaintiffs continued to bring securities class actions at elevated levels in 2020 — a sign that filings will remain high in the year ahead. Based on data from Cornerstone Research through September 30, 2020, plaintiffs were on pace to file approximately 375 federal and state securities class actions through the end of the year. Although lower than the more than 400 actions filed in each of the previous three years, this figure substantially exceeds the 261 cases brought, on average, between 2010 and 2019.

The moderate slowdown in filings is likely due to the pandemic, which led to widespread court closures and fewer mergers in the first half of 2020. The pandemic did, however, fuel its own cluster of event-driven cases, producing an estimated 16 securities-related actions through September 30. This represents the continuation of a development we observed in 2019 in event-driven litigation filings — matters where the catalyst is the disclosure or occurrence of a disaster or other serious event (*e.g.*, a wildfire, earthquake or cyberattack) that negatively impacts stock performance.

The panel also reported an uptick in cases against SPACs, entities formed for the purpose of acquiring privately held businesses, typically through reverse mergers. According to the industry website *SPACInsider*, there was an explosion of SPAC-related activity in 2020, with 248 IPOs, compared to 59 offerings in all of 2019. The offerings, referred to as "de-SPAC" transactions, have sparked a wave of securities actions in which investors claim to have been misled about facts bearing on the target's financial condition, prospects or operations. Bypassing litigation, some plaintiffs firms also have lodged behind-the-scenes demands, claiming that shareholders were misled by the issuer's regulatory filings and seeking curative disclosures in exchange for a quick settlement and attorneys' fees. Given the growing importance of SPACs, the panel expects to see more of these cases (and demands) in 2021.

Supreme Court's Shifting Composition Could Impact Securities Cases Going Forward

The panel observed that 2021 also may offer clues about whether the Supreme Court's evolving composition — including the recent appointment of Justice Amy Coney Barrett — will lead to a corresponding shift in its securities litigation jurisprudence.

While serving on the U.S. Court of Appeals for the Seventh Circuit, Justice Barrett did not author any opinions in securities cases. She was, however, an active participant during oral argument in *In re Allstate Corp. Securities Litigation*, 966 F.3d 595 (7th Cir. 2020), a Seventh Circuit decision that may hold relevance for *Arkansas Teachers Retirement System*, 955 F.3d 254 (2d Cir. 2020). The Court granted a petition for *certiorari* in *Arkansas Teachers* on December 10, 2020, and is scheduled to hear the case later this year.

On appeal from the U.S. Court of Appeals for the Second Circuit, *Arkansas Teachers* raises two questions involving class certification: (i) whether a defendant in a securities class action may rebut the classwide presumption of reliance recognized in *Basic Inc. v. Levinson* by pointing to the generic nature of the alleged misstatements (and their consequent failure to negatively impact the issuer's stock price) — even if that evidence also bears on the substantive element of materiality; and (ii) whether a defendant bears the burden of persuading the court on the lack of price impact.

In *Allstate*, the Seventh Circuit vacated a class certification order that was based, in part, on the district court's refusal to consider price impact evidence relating to the alleged misstatements. Although the Seventh Circuit acknowledged that Allstate's price impact theory "look[ed] very much like the prohibited defenses of no materiality," it nonetheless concluded that this "close similarity" did not allow the "district court to avoid a price impact defense at the class certification stage." The Seventh Circuit also held, like the Second Circuit in *Arkansas Teachers*, that defendants bear the burden of persuasion in rebutting *Basic*.

With Justice Barrett's elevation, these holdings could prove relevant when the Supreme Court considers *Arkansas Teachers* later this term. And looking ahead, President Trump's appointment of two other right-leaning justices, Neil A. Gorsuch and Brett M. Kavanaugh, suggests that Justice Barrett's conservative philosophy might carry influence if and when the Court considers other securities-related matters. Although theoretical, these are the kinds of issues that the panelists are thinking about as the Court ushers in a new era.

Lower Courts Continue To Wrestle With the Limits of Scheme Liability Post-*Lorenzo*

The panel also discussed several recent decisions applying *Lorenzo v. SEC*, 587 U.S. __, 139 S. Ct. 1094 (2019), in which the Supreme Court held that an individual could potentially be liable under Rules 10b-5(a) and (c) for disseminating to investors false statements prepared by someone else. Thus far, lower court interpretations of *Lorenzo* have focused narrowly on the factual allegations of each case, such as the defendant's relationship to the issuer and the significance of the defendant's role in the purported scheme.

As a result, decisions have gone both ways, making it difficult to identify clear trend lines. For instance, in *Geoffrey A. Orley Revocable Trust U/A/D 1/26/2000 v. Genovese*, 2020 WL 611506 (S.D.N.Y. 2020), the district court refused to impose liability on outside lawyers for their purported role in preparing allegedly misleading pitch documents. According to the court, because the lawyers were not accused of disseminating the statements, plaintiffs could not plead or prove reliance — an essential element in a private action under Section 10(b) and Rule 10b-5. This meant, in practical terms, that plaintiffs could "not take advantage of any additional liability Lorenzo may have carved out." By contrast, in *In re Cognizant Technology Solutions Corp. Securities Litigation*, 2020 WL 3026564 (D.N.J. 2020), the district court held that a corporate insider (in this case, the tech firm's chief legal officer) could potentially be held liable under Rules 10b-5(a) and (c) — irrespective of whether he engaged in actionable dissemination. One reason, the district court explained, was that the chief legal officer also had been accused of orchestrating the overall bribery scheme. Such allegations, in the district court's judgment, "plausibly indicate[d] that he [had] engaged in inherently deceptive conduct" falling within Rule 10b-5's ambit.

These decisions, along with several others, have brought a number of questions into sharper view. It appears, for instance, that plaintiffs are invoking Rules 10b-5(a) and (c) to target different kinds of behind-the-scenes actors — even if they neither have made nor disseminated the challenged statements. Will this continue? For her part, Ms. Gilden opined that the plaintiffs bar likely would continue to invoke *Lorenzo* in an effort to impose liability on different third-party actors. Relatedly, if plaintiffs continue to test the boundaries of scheme liability, will the need to plead the other elements of a primary violation (*e.g.*, scienter, reliance or loss causation) constrain their efforts at expansion? In this regard, the panel noted, the district court in *Takata v. Riot Blockchain, Inc.*, No. 18-02293 (FLW), 2020 WL 2079375 (D.N.J. Apr. 30, 2020), held that plaintiffs had adequately pled a deceptive act against one of the defendants under Rule 10b-5 yet still dismissed for lack of loss causation.

Second Circuit Weighs In on *Omnicare*'s Omissions Prong

The panel also examined two decisions in which the U.S. Court of Appeals for the Second Circuit applied the Supreme Court's test for opinion-based liability under an omissions theory. In the first appeal, *Abramson v. NewLink Genetics Corp.*, 965 F.3d 165 (2d Cir. 2020), the Second Circuit sustained claims based on opinions expressed by the company's CEO and chief medical officer. Examining the complaint's allegations, the court held that the plaintiff had alleged a concrete, objectively verifiable discrepancy between, on the one hand, a CEO's "confident statement" that no competing drug study had found a pancreatic cancer survival rate of more than 20 months, and on the other, his omission of findings from competing studies that had recorded survival rates well in excess of 20 months. By contrast, in *Shreiber v. Synacor*, No. 19-4232-cv, 2020 WL 6165909 (2d Cir. Oct. 22, 2020), the Second Circuit rejected claims that a technology company had misled investors about its anticipated revenues under a new contract. In contrast to the allegations in *NewLink Genetics*, the court observed, the plaintiffs in *Synacor* had failed to plead with specificity contemporaneous facts known to the company that plausibly contradicted its positive forecasts about the agreement's likelihood of success.

Together, these decisions offer guidance for interpreting the Supreme Court's seminal ruling in *Omnicare, Inc. v. Laborers District Council Construction Industries Pension Fund*, 575 U.S. 175 (2015). Writing for the majority in *Omnicare*, Justice Elena A. Kagan warned that meeting the Court's test under an omissions theory would be "no small task for an investor." *Id*. at 194. The decisions in *Newlink Genetics* and *Synacor* signal that while a plaintiff's burden in this area remains steep, there is a point at which an *Omnicare* defense becomes "a bridge too far." *Abramson*, 965 F.3d 165 (2d Cir. 2020). This holding calls for a case-by-case assessment and is not susceptible to bright-line rules. Nevertheless, it serves as a reminder that corporate issuers, along with their officers and directors, should proceed with caution when offering opinions. That means considering beforehand whether a particular view is, on balance, consistent with the universe of information within one's possession at the time.

Exclusive Federal Forum Provisions May Have a Meaningful Impact on Where '33 Act Claims Are Filed and Litigated

State court filings with Securities Act of 1933 ('33 Act) claims are on pace to fall for the first time since the Supreme Court's 2018 decision in *Cyan, Inc. v. Beaver County Employees Retirement Fund*, 583 U.S. --, 138 S. Ct. 1061 (2018). The panel noted that this decline may be traceable in part to the Delaware Supreme Court's 2020 decision in *Salzberg v. Sciabacucchi* (*Blue Apron II*), 227 A.3d 102 (Del. 2020), which held that Delaware corporations may include provisions in their certificates of incorporation requiring '33 Act claims to be brought in federal court. This highly anticipated decision will no doubt encourage more Delaware corporations to adopt exclusive federal forum provisions (FFPs).

Whether other state courts consistently uphold the validity of FFPs remains to be seen. Thus far, two California state judges — in *Wong v. Restoration Robotics, Inc.*, No. 18 CIV. 02609 (Cal. Super. Ct. Sept. 1, 2020), and *In re Uber Technologies, Inc. Securities Litigation*, No. CGC-19-579544 (Cal. Super. Ct. Nov. 16, 2020)— have enforced FFPs, albeit on grounds different than those laid out by the Delaware Supreme Court in *Blue Apron II*. (Both courts relied on principles of California — rather than Delaware — law.) If other jurisdictions do the same, FFPs could become a potent tool for eliminating duplicative litigation by steering '33 Act claims to the federal courts, where procedures exist for consolidation. Plaintiffs, however, have raised several legal objections — among them, that by enforcing FFPs, courts are impermissibly regulating interstate commerce in violation of the U.S. Constitution's Commerce Clause. This year may offer greater clarity about the viability of plaintiffs' constitutional and other challenges.

Case Law Developments Will Continue To Shape '33 Act Litigation Post-*Cyan*

Beyond FFPs, the panel will be tracking how litigants and trial courts react to two potentially impactful rulings from the First Department of New York State's Appellate Division. Since *Cyan* was decided in 2018, one recurring issue has been how to manage parallel proceedings in federal and state courts to avoid costly, duplicative litigation. One approach has been to seek a discretionary stay of the state action while the federal proceeding moves forward. In *Panther Partners Inc. v. Qudian Inc.*, No. 2020-02481, 2020 N.Y. Slip. Op. 07290 (1st Dep't, Dec. 3, 2020), the First Department reversed a lower court stay order that had been premised on an asserted overlap between parallel federal and state '33 Act claims. In its holding, the First Department emphasized that a decision in the non-stayed federal action would not have determined all of the claims pending in the state court action. Going forward, we anticipate that '33 Act plaintiffs — particularly in New York state court — will try to fit themselves within the scope of *Panther Partners* by attempting to distinguish their case from any first-filed parallel proceeding. This might mean filing unique claims or naming different parties as defendants — or both.

In another notable ruling, New York's Appellate Division reversed a trial court order and dismissed '33 Act claims stemming from the initial public offering (IPO) of Ruhnn Holding Limited, a recruiter, trainer and manager of social media influencers for China's e-commerce market. *See Lyu v. Ruhnn Holdings Ltd.*, 2020 NY Slip Op 07282 (App. Div. 1st Dep't Dec. 3, 2020). The plaintiffs alleged that Ruhnn was required to disclose updated numbers on store closings from the most recent quarter at the time of the IPO. In dismissing the complaint, the appellate court relied on the Second Circuit's decision in *Stadnick v. Vivint Solar*, 861 F.3d 31 (2d Cir. 2017), to conclude that the plaintiffs were viewing the store closings too "myopically." This is believed to be the first time that a New York state court has applied the Second Circuit's holistic standard for evaluating the accuracy of registration statements.

Ruhnn represents the first post-*Cyan* ruling by a New York appellate court and highlights a key feature of its procedural rules. Unlike in the federal system, where appeals generally must wait for a final judgment or order resolving all claims against all parties, defendants in New York state courts can immediately appeal the denial of a motion to dismiss. This distinction highlights a unique risk that plaintiffs face when opting for New York state court. Because a large number of '33 Act claims are typically filed in New York, the panel will be looking to see if *Ruhnn* has any impact going forward on plaintiffs' willingness to litigate in the Empire State.

Second Circuit's Decision on Remand in *Jander* May Make the Jurisdiction a Preferred Venue for ERISA Stock Drop Filings

The panel also examined the Supreme Court's failure to issue a ruling on the merits in *Retirement Plans Committee of IBM v. Jander*, 140 S. Ct. 592 (2020). The *Jander* appeal arose from a putative Employee Retirement Income Security Act of 1974 (ERISA) class action and raised an important threshold question: How strict should the pleading standard be for asserting claims against corporate insiders who serve as fiduciaries for employee stock ownership plans?

The central allegation in *Jander* was that plan administrators, all of whom were insiders, breached their fiduciary duties under ERISA by failing to disclose allegedly negative information about the purportedly impaired value of IBM's microelectronics business. According to the plaintiffs, these administrators should have understood not only that this nonpublic information would eventually be made public (allegedly because the business was about to be sold) but also that the resulting harm (*i.e.*, a drop in IBM's stock price) would only grow the longer the alleged fraud was concealed. As a result, the plaintiffs complained, any prudent fiduciary would have concluded that waiting to reveal the adverse information would do more harm than good.

In reversing the dismissal of the plaintiffs' complaint, the Second Circuit concurred that such generic allegations — *i.e.*, that disclosure of the fraud was inevitable and that stock price declines would increase over time — were sufficient to satisfy the "more harm than good" standard articulated by the Supreme Court's 2014 decision in *Fifth Third Bancorp v. Dudenhoeffer. See* 573 US 409 (2014). Despite granting certiorari in *Jander*, the Court declined to issue a decision on the merits and instead remanded the case to the Second Circuit. On June 22, 2020, the Second Circuit reinstated its original decision, effectively leaving intact what some have dubbed the court's "inevitable disclosure" pleading standard.

On November 9, 2020, the Supreme Court denied IBM's new petition for *certiorari*, cementing a circuit split that has continued to deepen. Indeed, last year, in *Allen v. Wells Fargo & Co.*, 967 F.3d 767 (8th Cir. 2020), the U.S. Court of Appeals for the Eighth Circuit rejected *Jander*'s test. In so holding, the court joined the Fifth, Sixth and Ninth circuits in ruling that generalized allegations, like those sustained in *Jander*, are legally infirm.

Unless and until the Supreme Court resolves the split, plaintiffs might begin filing ERISA stock drop cases more frequently in the Second Circuit, where they will claim, citing *Jander*, that the pleading standard is more challenging for defendants. In the interim, corporate defendants subject to personal jurisdiction in the Second Circuit may wish to consider whether it is worth mitigating the potential risks of *Jander* by relieving corporate insiders from their positions as ERISA plan fiduciaries. Since *Jander* applies only to officers serving in this dual capacity, such a preemptive measure would render the decision moot.

Ninth Circuit Clarifies Its Pleading Standards for Loss Causation While Reaffirming Its Common Sense Approach to Assessing Scienter

The panelists also reviewed several recent developments from the U.S. Court of Appeals for the Ninth Circuit in the areas of loss causation and scienter. This includes two 2020 decisions that offer guidance on the pleading standards for loss causation. In the first, a putative securities class action against BofI Holding, Inc., the court rejected a categorical rule that allegations from a separate whistleblower lawsuit, standing alone, can never qualify as a corrective disclosure. Instead, the court determined that such allegations can be deemed corrective when the complaint pleads facts from which to plausibly infer that "the market treat[ed] [the allegations] as sufficiently credible to be acted upon as truth." One month later, in a second appeal involving Bofl, the Ninth Circuit held that information obtained through a Freedom of Information Act (FOIA) request can be a corrective disclosure if it reveals new facts to the market. The court reasoned that because FOIA information is only disclosed by the government if requested, and because not all FOIA requests are granted, courts cannot assume for pleading purposes that information known to government regulators also is known to the market. Together, these decisions suggest that in at least two areas, involving whistleblower complaints and FOIA requests, courts should eschew bright-line rules in favor of a case-by-case assessment of the plaintiff's allegations.

In a third decision, *Nguyen v. Endologix, Inc.*, 962 F.3d 405 (9th Cir. 2020), the Ninth Circuit affirmed that the PSLRA not only permits but requires courts to engage in an holistic, common sense assessment of scienter. At issue in *Nguyen* was a statement by Endologix to the effect that it expected FDA approval of a new medical device. According to plaintiff, company officials made this statement with knowledge that, in fact, the FDA planned to reach the opposite conclusion and reject the product. The court, however, held that this theory of scienter was illogical and unsupported by well-pled facts. As the court explained, it would have made no sense for company officials to lie about the pendency of FDA approval if they knew that, eventually, their lie would be exposed. And this nonculpable inference was even more compelling, the court noted, because there were no allegations that any defendant sought to profit from their purported deception by executing insider trades. In the end, the Ninth Circuit concluded, plaintiffs were asking the court "to check [its] disbelief at the door," something "the PSLRA neither allows nor requires us" to do.

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