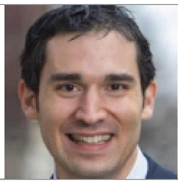
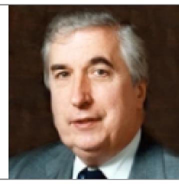


Insider Trading and Strategic Disclosure
By Joshua Mitts



Biden and the SEC: Some Possible Agendas
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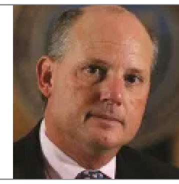

The Role of Institutional Investor Regulation in Restoring a Fair, Sustainable Economy
By Leo E. Strine, Jr.

THE CLS BLUE SKY BLOG
COLUMBIA LAW SCHOOL'S BLOG ON CORPORATIONS AND THE CAPITAL MARKETS

Skadden Discusses Trends in Securities Class Action Filings

By Jay B. Kasner, Scott D. Musoff, Susan L. Saltzstein and William J. O'Brien III March 9, 2021

Comment

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 is still substantially higher than 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 drop-off in M&A activity, in particular, led to a corresponding decline in federal merger objection lawsuits — a major contributor to overall filings since 2016. At the same time, the pandemic fueled its own cluster of event-driven cases, producing an estimated 16 securities-related actions through September 30, 2020. 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 significant event that negatively impacts stock performance.

The New Year May Usher in Even More Claims Against Non-US Issuers and SPACs

Securities filings against non-U.S. companies have continued to rise, with 35 such lawsuits initiated in the first half of 2020. If this pace continues, total filings for 2020 would exceed the prior record of 56, registered just one year earlier. Thus far, plaintiffs have focused substantially on Chinese firms that have delisted from U.S. exchanges (more than 60 since 2013). In the first half of 2020, 13 of the 35 suits against non-U.S. issuers fell into this category. In the Chinese issuer cases, a recurring theme has been the purported failure of these firms to disclose alleged violations of Chinese government regulations. (See “Hong Kong’s Exchange Improves Its Allure for Chinese Issuers.”)

We are also seeing an uptick in cases against special purpose acquisition companies. These companies, SPACs, are formed for the purpose of acquiring privately held businesses, typically through reverse mergers in which the operating entity or target survives and becomes a publicly traded issuer. According to the research firm Deal Point Data, there was an explosion of SPAC-related activity in 2020, with 247 IPOs, compared to 59 offerings in all of 2019. (See “The Year of the SPAC.”) 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 have also made behind-the-scenes demands, claiming that shareholders were deceived 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, we expect to see more of these cases (and demands) in 2021.

Exclusive Federal Forum Provisions and Case Law Developments Will Continue to Shape ’33 Act Litigation Post-*Cyan*

State court filings with Securities Act of 1933 (’33 Act) claims are on pace to decline for the first time since the U.S. Supreme Court’s 2018 decision in *Cyan, Inc. v. Beaver County Employees Retirement Fund*. Beyond the pandemic, this decline may be traceable in part to the Delaware Supreme Court’s 2020 decision in *Salzberg v. Sciabacucchi* (*Blue Apron II*), 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* and *In re Uber Technologies* — have enforced FFPs, albeit on grounds different from 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 follow suit, 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. The coming year may offer greater clarity about the viability of plaintiffs’ constitutional and other challenges.

In the meantime, we will monitor additional case law developments at the state court level. One threshold issue is whether plaintiffs can survive motions to dismiss. In a notable ruling from December 2020, 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. 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 U.S. Court of Appeals for the Second Circuit’s decision in *Stadnick v. Vivint Solar* 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.

The decision 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, we will be looking to see if *Ruhnn* has any impact going forward on plaintiffs’ willingness to litigate in the Empire State.

Shift in Supreme Court’s Composition Could Affect the Future Course of Securities Litigation Jurisprudence

The coming year may also offer clues about whether the U.S. 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. (See Insights Special Edition: US Supreme Court Term.)

Prior to joining the high court, Justice Barrett did not write or speak about topics related to securities litigation, either as a member of the U.S. Court of Appeals for the Seventh Circuit or as a professor at Notre Dame Law School. She did, however, join majority opinions in several securities and derivative cases, including one — *In re Allstate Corporation Securities Litigation* — that may shed light on how the Court could rule in a case before it this term, *Goldman Sachs Group Inc. v. Arkansas Teacher Retirement System* (*Arkansas Teachers*).

On appeal from the Second Circuit, *Arkansas Teachers* raises two questions involving class certification: (1) 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 (2) 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 become relevant when the Supreme Court considers *Arkansas Teachers* later this term. And looking ahead, Justice Barrett’s conservative philosophy may prove influential in several other contexts. To take one example, in the 2014 case *Halliburton Co. v. Erica P. John Fund, Inc.*, three justices — Clarence Thomas, Samuel A. Alito Jr. and Antonin Scalia — were poised to eliminate the *Basic* presumption of reliance altogether. Would Justice Barrett be willing to follow in the footsteps of her mentor, Justice Scalia, and consider overruling *Basic* if such a case were brought before the Court again? Although theoretical at this juncture, these are the kinds of issues that we will be looking out for as the Court ushers in a new, more conservative era.

Supreme Court’s Refusal to Grant Certiorari in *Jander* May Have Implications for ERISA Stock Drop Litigation

Courts may also have to deal with the implications of another Supreme Court decision, *Retirement Plans Committee of IBM v. Jander*. The January 2020 case is a putative Employee Retirement Income Security Act of 1974 (ERISA) class action that raises 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?

In *Jander*, the plaintiffs had accused plan administrators, all of whom were insiders, of violating 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 largely agreed with this framing of the "more harm than good" standard first enunciated in 2014 by the Supreme Court in *Fifth Third Bancorp v. Dudenhoeffer*. 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, in 2020, in *Allen v. Wells Fargo & Co.*, the U.S. Court of Appeals for the Eighth Circuit rejected *Jander*'s "inevitable disclosure" test and, in so holding, joined the Fifth and Sixth Circuits in ruling that generalized allegations of nondisclosure, such as those sustained in *Jander*, are legally infirm.

Unless and until the Supreme Court resolves the split, plaintiffs may 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.

Other Issues to Watch for in 2021

We also will be monitoring how the district courts adapt to other developments in the case law. This includes two 2020 decisions by the U.S. Court of Appeals for the Ninth Circuit 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 BofI, 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. In so holding, 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 is also known to the market.

Together, these decisions signal that at least in these 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.

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Given that securities filings remained at near-historic levels in 2020 despite the disruptions brought by the global pandemic, companies should expect the threat of potential litigation to remain high in 2021.

This post comes to us from Skadden, Arps, Slate, Meagher & Flom LLP. It is based on the firm's memorandum, "Despite Pandemic-Related Disruptions, Securities Class Action Filings Remain High With No Signs of Slowing," dated January 26, 2021, and available here.

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