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Cyan and the Future of Federal Securities Class Action Claims in State Court

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On May 23, 2017, the Acting Solicitor General weighed in on a closely watched petition for a writ of certiorari before the U.S. Supreme Court in *Cyan, Inc. v. Beaver County Employees Retirement Fund* concerning whether state courts have subject matter jurisdiction over class actions that exclusively allege federal claims under the Securities Act of 1933. In an amicus filing, the Acting Solicitor General accepted the Supreme Court's invitation to express the government's views on whether the petition for review should be granted as well as on the merits of the case.

The issue in *Cyan* concerns the interpretation of the Securities Litigation Uniform Standards Act of 1998 ("SLUSA"), which amended the federal securities laws, in part, "to stem the shift of class actions from federal to state courts." *Merrill Lynch, Pierce, Fenner & Smith Inc. v. Dabit*, 547 U.S. 71, 82 (2006). If the Supreme Court heeds the government's request to hear the case, the resulting decision could shift the jurisdictional landscape for securities class actions, and potentially resolve a schism among dozens of federal district courts throughout the country.

Cyan's Petition for Supreme Court Review

The *Cyan* petition arises from a decision of a California Superior Court, which denied the defendant company's motion for judgment on the pleadings. *Cyan* had argued that the state court lacked jurisdiction to hear the investors' allegations that the company had violated Section 11 of the Securities Act of 1933 by filing inaccurate and misleading offering documents in connection with its 2013 initial public offering. See 15 U.S.C. 77a *et seq.* In support of its motion, *Cyan* argued that SLUSA amended the Securities Act to remove state court jurisdiction over all "covered class actions," including actions that exclusively assert federal Securities Act claims. In denying *Cyan's* motion, the California Superior Court deferred to a 2011 California appellate decision, *Luther v. Countrywide Financial*, which held that SLUSA continued state-court jurisdiction over class actions brought exclusively under the Securities Act, and that only "covered class actions" asserting both Securities Act and state law claims were precluded from being litigated in state court. 125 Cal. Rptr. 3d 716 (Ct. App.), cert. denied, 565 U.S. 1080 (2011). *Cyan's* appeals to the California Court of Appeal and later the California Supreme Court were denied without opinion. Due to the procedural posture of the underlying case, the parties dispute whether the trial court's decision constitutes a final judgment

and thus whether the Supreme Court has jurisdiction to hear the petition. See 28 U.S.C. § 1257. Typically, the issue of whether a state court has subject matter jurisdiction over a federal Securities Act claim arises after defendants have tried to remove the case to federal court and a federal court remands the case to state court finding the state court has subject matter jurisdiction. Those decisions are not appealable and it is unlikely that any “final judgment” will find its way to the Supreme Court on this issue.

In their petition for writ of certiorari, the *Cyan* petitioners argue that precedent establishes the Supreme Court’s jurisdiction over the controversy and they contend that the California courts’ interpretation of SLUSA is contrary to both the statute’s text and purpose. Petitioners emphasize that SLUSA was enacted to end the pursuit of certain securities claims in state court, and thus prevent plaintiffs from evading the heightened standards and other reforms of the Private Securities Litigation Reform Act of 1995 (the “PSLRA”). The *Cyan* petitioners assert that SLUSA “eliminated state-court jurisdiction over class actions alleging [Securities] Act claims,” and thus the decision below “subverts both the [PSLRA] and SLUSA, to the detriment of national securities markets.” Petitioner’s Br. at 7, 23. Petitioners further urge that it is critical for the Supreme Court to hear this question, explaining that since 2011, following the *Luther* decision, state-court filings of class actions alleging only Securities Act claims have increased by an astounding 1400 percent. *Id.* at 8. In fact, due to the *Luther* decision, California superior courts have become a recent hotspot for Securities Act class action claims, where plaintiffs have sought to evade federal court jurisdiction.

Although the plaintiff investors initially declined to respond to the petition for review, the Supreme Court requested their reply. Following this request, Respondents defended the decision below as correct, because “[f]rom the earliest days of the federal securities laws, state courts have possessed concurrent jurisdiction over securities claims brought under both state law and the 1933 Act.” Respondents’ Br. at 1. Respondents further argue that the plain text of SLUSA did not create exclusive federal jurisdiction and allowing Securities Act claims to be litigated in state court “was completely consistent with the PSLRA.” *Id.* at 17.

The Supreme Court Asks the Acting Solicitor General to Weigh In

One month after the *Cyan* petition was fully briefed, the Supreme Court invited the Acting Solicitor General to file a submission expressing the views of the United States. The government’s recently filed amicus curiae brief expresses the government’s view that the *Cyan* petition for writ of certiorari should be granted, and that the Supreme Court has jurisdiction to hear the appeal. Brief for the United States as Amicus Curiae, at 1, 16-22. On the merits, the government takes the position that SLUSA’s text demonstrates that the California Superior Court “correctly held that SLUSA did not divest it of jurisdiction over respondents’ [Securities] Act suit.” *Id.* at 6. Even so, the Acting Solicitor General urges that Supreme Court “review is warranted to ensure that the statute is applied uniformly throughout the nation,” particularly in light of the “confusion in lower courts” on this question. *Id.* Notably, although the government takes the position that “respondents have the better of the interpretive dispute,” its amicus curiae brief acknowledges that a separate provision of SLUSA provides a statutory mechanism authorizing the removal of petitioner’s claims. *Id.* at 11, 13-14 (citing removal under Section 77(p)(c)).

Developments to Monitor

It remains an open question whether the Supreme Court will be persuaded by the briefs submitted by Petitioners and the Acting Solicitor General and agree to hear the case next term. Nonetheless, it is noteworthy both that the Supreme Court called for the views of the Solicitor General and that the Acting Solicitor General recommended that the Supreme Court grant certiorari. A decision by the Supreme Court on this issue would help resolve the clear divide among federal district courts on the issue: at least fifteen different federal district courts have held that state courts have subject matter jurisdiction over cases solely involving federal Securities Act claims, while at least a dozen other federal district courts have held the opposite. In the absence of any decision, defendants who find themselves faced with a complaint alleging federal securities claims in state court must continue to pay careful attention to the widening split among federal district courts.

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