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PERSPECTIVE

Securities Act cases are surging... in state courts?

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For years, state courts have languished as a jurisdiction for the filing of claims under the Securities Act of 1933, which imposes liability for material misstatements or omissions in registration statements. However, a series of unexpected developments in jurisprudence and regulation may be turning this settled landscape on its head.

There were 288 initial public offerings completed in the U.S. in 2014, a 27 percent increase over 2013 (225 IPOs), and is the highest number of U.S. IPOs since 2000. This pace has continued through the first half of 2015.

The rise in IPO activity is due, at least in part, to the "IPO on-ramp procedures" in the Jumpstart Our Business Start-Ups (JOBS) Act of 2012, which eased the process of going public for "emerging growth companies," or companies with annual revenues less than $1 billion. While the JOBS Act may have eased the registration process for smaller companies by loosening certain disclosure and financial reporting requirements, the same changes have resulted in far less transparency for investors — sometimes leading to very unpleasant surprises.

Since the passage of the JOBS Act, there has been a distinct rise in securities class actions against newly public companies. Shareholders filed nearly 50 percent more class actions over unsuccessful IPOs in 2014 than 2013, or 19 filings compared to 13 the year before. Through the first half of 2015, there have been a total of 13 Securities Act lawsuits filed against IPO companies (out of 91 total securities suits filed), representing about 14 percent of all first half filings. Of the 13 new lawsuits filed against IPO companies during the first half of 2015, five were filed in state courts — four in California and one in New York.

The fact that plaintiffs are now able to bring federal Securities Act lawsuits in California state court and keep them there is the result of a hotly contested point of statutory interpretation. Section 22(a) of the Securities Act generally provides for concurrent state court jurisdiction for civil actions alleging a violation of the Securities Act's liability provisions. Known as the "removal bar," Section 22(a) also provides that no action properly filed in stated court "shall be removed to any court of the United States."

As part of a series of reforms designed to curb frivolous litigation, Congress in 1998 passed the Securities Litigation Uniform Standards Act (SLUSA), which enabled defendants to remove to federal court "covered class actions" (those involving 50 or more class members), thus subjecting certain plaintiffs to heightened federal restrictions on securities class actions.

The fact that plaintiffs are now able to bring federal Securities Act lawsuits in California state court and keep them there is the result of a hotly contested point of statutory interpretation.

In the years following SLUSA, courts split on whether Securities Act claims were subject to SLUSA's removal provision. Certain defendants argued, and some courts concluded, that SLUSA amended the Securities Act's jurisdictional provision, divesting state courts of concurrent jurisdiction over class actions asserting Securities Act claims.

Despite this inconsistency, plaintiffs have enjoyed considerable success in avoiding removal in California state courts. The primary reason for this success is dicta from the 9th U.S. Circuit Court of Appeals' decision in *Luther v. Countrywide Home Loans Servicing LP*, 533 F.3d 1031 (2008), where the court concluded that the Securities Act "strictly forbids the removal of cases brought in state court and asserting claims under the Act." Consistent with the 9th Circuit's recognition that the Securities Act provides concurrent state court jurisdiction, virtually all California federal district courts have remanded cases arising under the Securities Act back to state court.

The landscape for securities class action litigation is constantly shifting. With the proliferation of IPOs showing no signs of cooling off, securities class actions filed in state court will almost certainly continue.

Lawyers will continue to disagree on SLUSA's effect on state court jurisdiction unless and until a federal appeals court squarely addresses SLUSA's effect on state court jurisdiction and removal of Securities Act class actions. In the interim, the absence of any Court of Appeals or Supreme Court authority will allow plaintiffs to continue filing these actions, primarily in California state courts, while avoiding jurisdictions that lack clear guidance.

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