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UNINTENDED CONSEQUENCES, LOOPHOLES, AND GIBBERISH: WHY THERE ARE STILL SECURITIES ACT CLASS ACTIONS IN STATE COURTS

*By: Brian Elzweig**

Abstract

This Article examines Congress's decades-long attempt to ensure that securities class action lawsuits of national importance are litigated in federal courts. The intent is limiting strike suits. Congress attempted to curtail strike suits through the enactment of the Private Securities Litigation Reform Act ("PSLRA"). The PSLRA required heightened pleading requirements to ensure the validity of federal securities class actions. Instead of solving the dilemma, plaintiffs circumvented the PSLRA by bringing fraud cases as state law claims. To combat the circumvention of the PSLRA, Congress enacted the Securities Litigation Uniform Standards Act ("SLUSA"). SLUSA federally preempted state law claims based on alleged misrepresentations, untrue statements, or omissions of material facts, requiring them to be brought in federal court. However, SLUSA did not address the concurrent jurisdiction provision of the Securities Act of 1933. This created an anomaly whereby many federal claims under the 1933 Act were brought in state courts, while state fraud claims were required to be brought in federal court. Congress could have addressed this enigma when it enacted the Class Action Fairness Act ("CAFA"). Instead, CAFA, which reformed class actions generally, exempted most securities class actions from its rules. In 2018, the Supreme Court decided Cyan v. Beaver County *and allowed 1933 Act claims covered by SLUSA to continue to be brought in state courts. The Court was silent on non-covered securities. This Article recommends how Congress can accomplish its goal of forcing important securities class actions into federal courts.*

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I. Introduction

In 2018, the Supreme Court issued its ruling in *Cyan v. Beaver County Retirement Fund*, affirming that class actions could be brought in state court if they were based on allegations of violations of the Securities Act of 1933 ("1933 Act") and they were covered securities under the Securities Litigation Uniform Standards Act ("SLUSA").[1] Class action lawsuits have long been a way for multiple plaintiffs with similar damages against the same defendant to engage in collective litigation.[2] This saves time and reduces duplication of resources by allowing one plaintiff to act on behalf of the class and then split the damages among all the defendants.[3] This has been an especially useful tool in securities litigation because many shareholders often fall victim to the same misdealing by a corporation in which they own stock. The broad anti-fraud provisions in the 1933 Act and Securities Exchange Act of 1934 ("1934 Act") often served as the basis for these class actions as both acts create a private right of action.[4] Subsequent to the enactment of these two acts, many allegations of class action abuse arose, claiming that the class action attorneys were creating strike suits with little benefit to the plaintiffs but creating high fees for the attorneys.[5] Further, it was alleged that people were filing class action lawsuits based on a drop in stock value without having any evidence of misdoing by the company.[6] To curb these abuses, Congress enacted the Private Securities Litigation Reform Act ("PSLRA") in 1995.[7] The PSLRA added heightened pleading requirements and changed class certification standards. The PSLRA, however, had the unintended consequence of pushing cases to state courts so litigants could avoid these changes. Litigants would file class actions in state courts alleging either state law violations or violations of the 1933 Act, which

1. Cyan, Inc. v. Beaver Cty. Emps. Ret. Fund, 138 S. Ct. 1061, 1066 (2018).
2. Susan T. Spence, *Looking Back . . . In a Collective Way: A Short History of Class Action Law*, 11 A.B.A. Sec. Bus. L. Rep. 6 (2002).
3. *Id.*
4. Doug Greene, Jessie Gabriel, Marco Molina & Brian Song, *The Coming Securities Class Action Storm: Multijurisdictional Litigation After* Cyan, 32 Plus J. 1 (2018), https://www.wileyrein.com/media/publication/486_Q32018.pdf [https://perma.cc/NF3B-FE79].
5. *See* S. Rep. No. 104-98, at 4 (1995).
6. *Id.*
7. Private Securities Litigation Reform Act, Pub. L. No. 104-67, 109 Stat. 737 (1995) (codified in scattered sections of 15 U.S.C.).

allows for concurrent federal and state jurisdiction. Plaintiffs often engaged in forum shopping to file their cases in what they considered plaintiff-friendly states.[8] Thus, the PSLRA was generally ineffective at curbing class action abuse.[9]

Congress responded in 1998 by passing SLUSA[10] to quell state court securities class actions. SLUSA sought to enact national standards for securities litigation. It did this by creating federal preemption over cases that alleged misrepresentation, untrue statements, or omissions of material facts. Federal courts required the heightened standards set forth in the PSLRA. However, while SLUSA was clear that federal preemption existed over state law claims, it did not address the concurrent jurisdiction provision in the 1933 Act.[11] Therefore, it was unclear if SLUSA amended the 1933 Act—thus forcing 1933 Act claims to be litigated in federal court.[12] This lead to inconsistent results at the district court level. In some circuits, federal district courts required that state law claims be brought in federal court, but allowed federal law claims under the 1933 Act to be brought in state court.[13] District courts in other circuits required 1933 Act claims covered by SLUSA to be litigated in federal court.[14] This split eventually led to the *Cyan* decision, which attempted to determine the proper interpretation of SLUSA's jurisdictional requirements, which Justice Alito called "gibberish."[15]

In 2005, Congress again reformed class action litigation by enacting the Class Action Fairness Act ("CAFA").[16] CAFA was designed to require all class actions of national interest to be litigated in federal courts. Because Congress had addressed securities reform in the PSLRA and SLUSA, CAFA exempted cases involving covered securities.[17] This created another loophole leading to forum shopping. The Ninth Circuit, when examining the interplay between CAFA and SLUSA, allowed cases involving 1933 Act claims on non-covered se-

8. Michael A. Perino, *Fraud and Federalism: Preempting Private State Securities Fraud Causes of Action*, 50 STAN. L. REV. 273, 311 (1998).

9. S. REP. NO. 104-98, at 1 (1995).

10. Securities Litigation Uniform Standards Act of 1998, Pub. L. No 105-353, 112 Stat. 3227 (1998) (codified in scattered sections of 15 U.S.C.).

11. Mitchell A. Lowenthal & Shiwon Choe, *State Courts Lack Jurisdiction to Hear Securities Act Class Actions, But the Frequent Failure to Ask the Right Question Too Often Produces the Wrong Answer*, 17 U. PA. J. BUS. L. 739, 744–45 (2015).

12. *Id*. at 745.

13. Matthew O'Brien, *Choice of Forum in Securities Class Actions: Confronting "Reform" of the Securities Act of 1933*, 28 REV. LITIG. 845, 862 (2009).

14. *Id*.

15. Transcript of Oral Argument at 11, Cyan v. Beaver Cty. Emps. Ret. Fund, 138 S. Ct. 1061 (2018) (No. 15-1439) [hereinafter Transcript of Oral Argument].

16. Class Action Fairness Act of 2005, Pub. L. No. 109-2, 119 Stat. 4 (2005) (codified in scattered sections of 28 U.S.C.).

17. Jeffrey T. Cook, *Recrafting the Jurisdictional Framework for Private Rights of Action Under the Federal Securities Laws*, 55 AM. U. L. REV. 621, 622 (2006).

curities to be litigated in state court.[18] The Seventh Circuit took the opposite approach and required all 1933 Act claims meeting CAFA's jurisdictional requirements to be litigated in federal court.[19] This split allowed another avenue to use forum shopping to bring a securities class action in state court.

This Article traces the long history of securities class action litigation. It examines how plaintiffs have tried to find ways to litigate these cases in state courts, and how Congress has tried to federally preempt securities class actions. It has been judicially determined that some 1933 Act claims may be litigated in state courts—leaving opportunities for forum shopping.[20] This Article examines whether this consequence conflicts with Congress's intent and makes recommendations to prevent future litigation in state courts. Part II discusses the history of securities class actions, including the first recognition of private rights of action for securities lawsuits, as well as the jurisdictional anomalies present in the early securities class action statutes. Part III provides a background of class action litigation generally, from its early roots in England to its recognition as a viable and efficient means of litigation in the United States. Part IV examines the rise of securities class action litigation, while Part V analyzes Congress's various attempts to curb the increasing abuse. Part VI examines the Supreme Court's recent decision in *Cyan* and its likely impact and unintended consequences.

II. The History of Securities Class Actions

A. *Private Rights of Action*

Shortly after the stock market crash of 1929, Congress enacted two major pieces of legislation to protect investors by promoting honesty and fairness in the United States securities markets. The first of these acts was the 1933 Act.[21] The 1933 Act requires that those who initially introduce securities into the market give "full and fair disclosure of information to the public in the sales of [those] securities."[22] The following year, Congress passed the 1934 Act.[23] In contrast to the 1933 Act, the 1934 Act is "chiefly concerned with the regulation of post-distribution trading on the [n]ation's stock exchanges and securities trading markets."[24] The purpose is to prevent fraud in securities trans-

18. *See* Luther v. Countrywide Home Loans Servicing LP, 533 F.3d 1031 (9th Cir. 2008).
19. *See* Katz v. Gerardi, 552 F.3d 558 (7th Cir. 2009).
20. *See, e.g.*, Cyan, Inc. v. Beaver Cty. Emps. Ret. Fund, 138 S. Ct. 1061, 1072–73 (2018).
21. 15 U.S.C. § 77 (2012).
22. Pinter v. Dahl, 486 U.S. 622, 646 (1988).
23. 15 U.S.C. § 78 (2012).
24. Blue Chip Stamps v. Manor Drug Stores, 421 U.S. 723, 752 (1975).

actions after the initial issuance of securities.[25] Both the 1933 Act and the 1934 Act have broad antifraud provisions. Section 11 of the 1933 Act creates a private right of action allowing for a person acquiring a security to sue if the registration statement contains an untrue statement of material fact or an omission of a material fact.[26] The same section authorizes the person who acquired the security to sue every person who signed the registration statement, every person who was a director or partner of the security issuer at the time the registration statement was filed, every person named in the registration statement as about to become a director, every accountant, engineer, or appraiser, and every underwriter with respect to the security.[27]

Section 12(a)(2) of the 1933 Act has a similar provision creating liability for anyone who "by means of a prospectus or oral communication, which includes an untrue statement of a material fact or omits to state a material fact necessary in order to make the statements, in the light of the circumstances under which they were made, not misleading."[28]

Similarly, the 1934 Act also contains a broad antifraud provision in section 10(b). It states that:

> It shall be unlawful for any person, directly or indirectly, by the use of any means or instrumentality of interstate commerce or of the mails, or of any facility of any national securities exchange . . . [t]o use or employ, in connection with the purchase or sale of any security . . . any manipulative or deceptive device or contrivance in contravention of such rules and regulations as the Commission may prescribe as necessary or appropriate in the public interest or for the protection of investors."[29]

Thus, the 1934 Act gave the Securities and Exchange Commission ("SEC") the power to promulgate rules to prevent fraudulent acts regarding sales of securities.[30] The SEC responded to this power by promulgating Rule 10b-5. Rule 10b-5 provides a broad range of what is considered to be fraudulent under the 1933 Act. Rule 10 b-5 makes it:

> unlawful for any person, directly or indirectly, by the use of any means or instrumentality of interstate commerce, or of the mails or of any facility of any national securities exchange,
> (a) To employ any device, scheme, or artifice to defraud,
> (b) To make any untrue statement of a material fact or to omit to state a material fact necessary in order to make the statements made, in the light of the circumstances under which they were made, not misleading, or

25. Cyan, Inc. v. Beaver Cty. Emps. Ret. Fund, 138 S. Ct. 1061, 1066 (2018).
26. 15 U.S.C. § 77k(a) (2012).
27. *Id.*
28. 15 U.S.C. § 77l(a)(2) (2012).
29. 15 U.S.C. § 78(j) (2012).
30. 15 U.S.C. § 78j(b) (2012).

> (c) To engage in any act, practice, or course of business which operates or would operate as a fraud or deceit upon any person,
> in connection with the purchase or sale of any security.[31]

To help further the purpose of the 1933 Act, Congress allowed "any person" who acquired a security to bring a case under the antifraud provision.[32] In doing so, Congress explicitly created a private cause of action for a person who acquired a security that was issued in violation of the Act. In contrast, no such right is explicitly stated in the 1934 Act. However, the courts construing section 10(b) and Rule 10b-5 concluded that Congress intended to create a private remedy for violations of those acts as well.[33] A federal court first recognized a private right of action under Rule 10b-5 in 1946, which was just four years after the adoption of the rule.[34] In that case, *Kardon v. National Gypsum Company*, the court allowed a private plaintiff to bring an action for being induced by a conspiracy to sell stock for less than its value.[35] The court in *Kardon* recognized that neither section 10(b) nor Rule 10b-5 explicitly recognized a private right of action.[36] However, it opined that without a private right of action, the plaintiffs would have no remedy.[37] While Congress may make a rule in which a plaintiff would have no remedy, the court noted that any intention to do so "should appear very clearly and plainly."[38] Once *Kardon* recognized a private right of action, its holding was adopted by other courts. Eventually, in 1971, the Supreme Court first recognized a private right of action under the 1934 Act in *Superintendent of Insurance v. Bankers Life & Casualty Company*.[39] In a footnote, the Court stated without explanation that "[i]t is now established that a private right of action is implied under [section] 10(b)."[40] Since then, the Court has repeatedly recognized this private right of action.[41] In addition, the Court noted private actions provide "a most effective weapon in the enforcement"

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31. 17 C.F.R. § 240.10b-5 (2007).
32. 15 U.S.C. § 77k(a) (2012).
33. Scott M. Murray, Cent. Bank of Denver v. First Interstate Bank of Denver: *The Supreme Court Chops a Bough from the Judicial Oak: There is No Implied Private Remedy to Sue for Aiding and Abetting Under Section 10(b) and SEC Rule 10b-5*, 30 New Eng. L. Rev. 475, 484–85 (1996).
34. *Id.* at 485.
35. Kardon v. Nat'l Gypsum Co., 69 F. Supp. 512, 513 (E.D. Pa. 1946).
36. *Id.*
37. *Id.*
38. *Id.* at 514.
39. Superintendent of Ins. v. Bankers Life & Cas. Co., 404 U.S. 6, 13 (1971).
40. *Id.* at 13 n.9.
41. *See, e.g.*, Chadbourne & Parke LLP v. Troice, 571 U.S. 377, 382 (2014); Amgen Inc. v. Conn. Ret. Plans & Tr. Funds, 568 U.S. 455, 487 (2013); Merrill Lynch, Pierce, Fenner & Smith Inc. v. Dabit, 547 U.S. 71, 84 (2006); Blue Chip Stamps v. Manor Drug Stores, 421 U.S. 723, 730 (1975).

of the securities laws and are "a necessary supplement to Commission action."[42]

B. *Concurrent Jurisdiction of the 1933 Act*

While both the 1933 Act and the 1934 Act allow for private rights of action, they differ in federal and state jurisdiction. Section 22(a) of the 1933 Act authorized concurrent jurisdiction between federal and state courts of "all suits brought to enforce any liability or duty" created by the Act.[43] Additionally—and rather unusually—along with concurrent jurisdiction, the 1933 Act also has an anti-removal provision.[44] Section 22(a) states that "[n]o case arising under this title and brought in any State court of competent jurisdiction shall be removed to any court of the United States."[45] This allows a plaintiff the choice to bring a 1933 Act case in state court without the defendant having the ability to remove it to federal court.[46] These two mechanisms in section 22(a) are designed to be friendly to the plaintiff.[47] They allow plaintiffs bringing 1933 Act claims to ultimately choose the forum in which the case is litigated.[48]

The 1934 Act does not have a jurisdictional provision like the one in section 22(a) of the 1933 Act. While allowing for private rights of action, the 1934 Act confers only federal jurisdiction on cases brought under the statute.[49] Section 27 of the 1934 Act states:

> the district courts of the United States . . . shall have exclusive jurisdiction of violations of this chapter or the rules and regulations thereunder, and of all suits in equity and actions at law brought to enforce any liability or duty created by this chapter or the rules and regulations thereunder.[50]

This provision limited those suing for violating the 1934 Act (or rules that arise under its provisions) from litigating the case in a state court.[51] Interestingly, Congress contemplated exclusive federal jurisdiction for the 1933 Act as well, but ultimately chose to allow concurrent jurisdiction.[52] The reasons for the disparity in the jurisdictional

42. Bateman Eichler, Hill Richards, Inc. v. Berner, 472 U.S. 299, 310 (1985) (quoting J.I. Case Co. v. Borak, 377 U.S. 426, 432 (1964)).

43. 15 U.S.C § 77v(a) (2012).

44. Cyan, Inc. v. Beaver Cty. Emps. Ret. Fund, 138 S. Ct. 1061, 1066 (2018).

45. 15 U.S.C. § 77v(a) (2012).

46. *Cyan*, 138 S. Ct. at 1066.

47. Denise Mazzeo, *Securities Class Actions, CAFA, and a Countrywide Crisis: A Call for Clarity and Consistency*, 78 FORDHAM L. REV. 1433, 1443–44 (2009).

48. Stephen O'Connor, *The Securities Act of 1933: A Jurisdictional Puzzle*, 79 BROOK. L. REV. 1233, 1239 (2014).

49. 15 U.S.C. § 78aa(a) (2012).

50. *Id.*

51. *Cyan*, 138 S.Ct. at 1066.

52. Mazzeo, *supra* note 47, at 1444 (citing 78 CONG. REC. 8563, 8571 (1934) (statement of Sen. Byrnes)).

standards are unclear.[53] There is a dearth of legislative history as to why section 22 of the 1933 Act contains the anti-removal provision.[54] This is surprising because of the rarity of anti-removal provisions in federal law.[55]

The antifraud provisions of the 1933 and the 1934 Acts became the cornerstone of securities class action litigation. With both allowing for private rights of action, purchasers of securities could individually sue issuers and resellers of securities and seek damages. This obviated the need for intervention by the SEC for such lawsuits. Today, modern securities class actions are also known for reducing redundant lawsuits because often many people are aggrieved in the same way by the same issuer in securities fraud cases. However, to fully understand the goal of class actions, some background history on class action litigation in general is helpful.

III. The History of Class Action Litigation

The roots of class action litigation go back to early English law, likely as far back as an 1199 case called *Master Martin Rector of Barkway v. Parishioners of Nuthampstead*.[56] The case involved collective litigation by a parish rector against multiple parishioners to collect parochial fees.[57] Four parishioners brought the case on behalf of the rest of the petitioners in the court of the Archbishop of Canterbury.[58] This allowed for the rector to litigate his claims over charges for and locations of burials against the entire parish with four representative plaintiffs.[59]

The earliest cited example of a judicially-created class action arose in a 1309 case entitled *Discart v. Otes*.[60] This case entailed a man who lived in the Channel Islands.[61] The Channel Islands were Norman by heritage, but after the Norman Conquest they became subject to English rule.[62] Subsequently, King Edward I granted ownership of the Channel Islands to Sir Otes Grandison.[63] Otes decreed that all money due to him or to the crown be paid in French currency instead of the local coinage of the Channel Islands. Jordan Discart was a granger for the king and owed the crown a commission on the sale of corn.[64] Dis-

53. O'Connor, *supra* note 48, at 1240.
54. Mazzeo, *supra* note 47, at 1443.
55. *Id.*
56. Spence, *supra* note 2.
57. Stephen C. Yeazell, *The Past and Future of Defendant and Settlement Classes in Collective Litigation*, 39 Ariz. L. Rev. 687, 688 (1997).
58. *Id.*
59. *Id.*
60. Raymond B. Marcin, *Searching for the Origin of the Class Action*, 23 Cath. U. L. Rev. 515, 521 (1974).
61. Spence, *supra* note 2.
62. *Id.*
63. *Id.*
64. *Id.*

cart made the commission payments in the local currency of the Channel Islands. However, Otes demanded that Discart pay the commission in French currency instead.[65] Discart was not the only person who wanted to pay such fees in the local currency,[66] so he filed a bill to have the dispute resolved with the justices in General Eyre of the Channel Islands.[67] The justices of the General Eyre avoided deciding the case and instead referred that matter to the King's Council. In doing so, the justices required that Discart and "all that are in like case with [Discart were] bidden to appear . . . before that same Council, either in person or by someone representing them all, to hear its opinion and to receive such judgment as shall there be delivered."[68] Thus, the justices of the General Eyre created the first known class action.[69]

The 1820 case of *West v. Randall*[70] is recognized as the first class action in the United States.[71] It was brought in the United States Court of Appeals for the Circuit of Rhode Island, which now is the United States Court of Appeals for the First Circuit.[72] *West* involved a dispute over an accounting of property conveyed by William West to one of his heirs.[73] The heir brought an action against the survivors of four trustees to account for property conveyed to them to pay West's debts.[74] The heir claimed a portion of West's estate. However, West's other heirs and his personal representative were not made parties to the lawsuit.[75] In response to the lawsuit, the defendants named other heirs and alleged that they were within the jurisdiction of the court.[76] Applying general rules of equity, the court noted "that all persons materially interested, either as plaintiffs or defendants in the subject matter of the bill ought to be made parties to the suit, however numerous they may be."[77] The case, however, did not indicate that parties who were absent would be bound by the lawsuit.

In 1842, the Supreme Court issued new Federal Equity Rules. Rule 48 stated:

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65. *Id.*

66. *Id.*

67. *Id.*

68. *Id*. (quoting Discart v. Otes, 30 Seld. Society 137 (No. 158, P.C. 1309) (1914)).

69. *Id.*

70. West v. Randall, 29 F. Cas. 718 (C.C.D.R.I. 1820) (No. 17,424).

71. Howard M. Downs, *Federal Class Actions: Due Process by Adequacy of Representation (Identity of Claims) and the Impact of* General Telephone v. Falcon, 54 OHIO ST. L.J. 607, 621 n.55 (1993).

72. J. Britton Whitbeck, *Identity Crisis: Class Certification, Aggregate Proof, and How Rule 23 May Be Self-Defeating the Policy for Which It Was Established*, 32 PACE L. REV. 488, 489 (2012).

73. *West*, 29 F. Cas. at 721.

74. *Id.*

75. *Id.*

76. *Id.*

77. *Id.*

> Where the parties on either side are very numerous, and cannot, without manifest inconvenience and oppressive delays in the suit, be all brought before it, the court in its discretion may dispense with making all of them parties, and may proceed in the suit, having sufficient parties before it to represent all the adverse interests of the plaintiffs and the defendants in the suit properly before it. But in such cases the decree shall be without prejudice to the rights and claims of all the absent parties.[78]

Rule 48 allowed for collective litigation, but did not form true class actions because the class did not represent parties who were absent in the litigation. The Supreme Court examined collective litigation in 1853 in a case styled *Smith v. Swormstedt*.[79] *Smith* involved a group of traveling preachers dissociating from the Methodist Episcopal Church.[80] Differences within the church about slavery led to a division in the church, creating two separate entities: the Methodist Episcopal Church South and the Methodist Episcopal Church North.[81] The church, prior to the division, had a fund called the Book Concern. The southern branch of the church argued that they were promised shares of the Book Concern, and that the promise partially induced them to separate.[82] The northern division argued that the case did not include all of the proper parties. The southern division alleged that 1,500 preachers were affected and that each had an interest in the Book Concern. Because of the number of plaintiffs, some argued it was "impossible . . . to make them all parties to the bill."[83] The Court noted that:

> The rule is well established, that where the parties interested are numerous, and the suit is for an object common to them all, some of the body may maintain a bill on behalf of themselves and of the others; and a bill may also be maintained against a portion of a numerous body of defendants, representing a common interest.[84]

By allowing the case to proceed with a portion of the plaintiffs representing the others in the litigation, the Court confirmed that class action litigation could occur. However, there was still doubt as to whether absent class members would be bound by the judgment of a court hearing a class action.[85] When the Court adopted the Rules of Civil Procedure in 1937, it codified class action procedure.[86] Rule 23 established the requirements and procedures for federal class action

78. FED. EQUITY R. 48, 42 U.S. lvi (1842) (repealed 1912).
79. Smith v. Swormstedt, 57 U.S. 288 (1853).
80. *Id.* at 298–99.
81. *Id.*
82. *Id.* at 300.
83. *Id.*
84. *Id.* at 302.
85. Spence, *supra* note 2.
86. *Id.*

litigation, ushering in the era of modern class actions.[87] In 1966, amendments to Rule 23 bound absent members to class action judgments.[88] States also adopted rules for state class action procedures, allowing states to have collective litigation as well.

IV. Increase in Number of Securities Class Actions

Class actions are often the primary mechanism for shareholders to enforce their rights against corporate misconduct.[89] Class actions are appropriate in securities cases as they often involve a large number of plaintiffs whose claims can be aggregated.[90] Class actions also give these plaintiffs an economically viable option to litigate cases that would not make sense to bring individually.[91] By 2006, securities litigation made up 40% of all federal class action litigation.[92] These cases accounted for 76% of the ascertainable money value for settlements of all federal class actions that year.[93] Because of their broad coverage, traditionally most federal class action securities lawsuits arise, at least in part, from section 10 of the 1934 Act and SEC Rule 10b-5.[94] A private right under Rule 10b-5 is similar to, but not identical to, a common law deceit and misrepresentation action.[95] To establish a private Rule 10b-5 fraud action, a plaintiff must prove six elements. These elements are: (1) a material misrepresentation or omission of a material fact; (2) scienter; (3) a connection with the purchase or sale of securities; (4) reliance; (5) economic loss; and (6) loss causation.[96]

Securities fraud class action litigation became more frequent after 1988.[97] This is primarily because of the Supreme Court's decision in *Basic v. Levinson*.[98] *Basic* focused on the element of reliance. Basic Inc. ("Basic") was a manufacturing company that made refractories for the steel industry.[99] A company called Combustion Engineering, Inc. ("Combustion") had expressed interest in acquiring Basic.[100] In 1976, Combustion's Industrial Products Group strategic plan included

87. Fed. R. Civ. P. 23.
88. Spence, *supra* note 2.
89. Stephen E. Morrissey, *State Settlement Class Actions That Release Exclusive Federal Claims: Developing a Framework for Multijurisdictional Management of Shareholder Litigation*, 95 Colum. L. Rev. 1765, 1765 (1995).
90. *Id.*
91. *Id.*
92. Brian T. Fitzpatrick, *An Empirical Study of Class Action Settlements and Their Fee Awards*, 7 J. Empirical Legal Stud. 811, 818 (2010).
93. *Id.* at 825.
94. Greene et al., *supra* note 4, at 1–2.
95. Dura Pharm., Inc. v. Broudo, 544 U.S. 336, 341 (2005).
96. *Id.* at 341–42.
97. *Congress, The Supreme Court, and the Rise of Securities-Fraud Class Actions*, 132 Harv. L. Rev. 1067, 1067 (2019).
98. Basic v. Levinson, 485 U.S. 224 (1988).
99. *Id.* at 226.
100. *Id.*

an objective to acquire Basic for $30 million.[101] In the same year, Basic and Combustion's executives had meetings concerning the possibility of a merger.[102] During 1977 and 1978, Basic made three public statements denying that it was engaged in merger negotiations.[103] On December 18, 1978, Basic had the New York Stock Exchange suspend trading of its stock and issued a statement entailing that it was approached by another company concerning a merger.[104] The next day, Basic's board of directors announced that it supported an offer by Combustion to purchase its stock for $46 per share.[105] One day later, Basic's board approved of Combustion's tender offer to buy all of Basic's outstanding shares.[106] The plaintiffs were former Basic shareholders who sold their stock after Basic first denied that they were engaged in merger talks and before trading of its stock was suspended in December 1978.[107] They claimed that Basic's denials of the merger talks were misleading and therefore violated section 10(b) of the 1934 Act and Rule 10b-5.[108]

Basic argued that the plaintiffs could not certify a class in the action because each plaintiff would have had to individually rely on the statements of Basic's board.[109] Prior to *Basic*, the reliance element of a 10b-5 claim could usually only be established if each individual plaintiff knew of and traded securities based on a specific falsehood.[110] This argument would make it hard for a class to be certified because individual reliance issues were almost never the same among a class.[111]

Instead, the Court adopted the fraud-on-the-market theory, summarized in *Basic* as:[112]

> in an open and developed securities market, the price of a company's stock is determined by the available material information regarding the company and its business . . . . Misleading statements will therefore defraud purchasers of stock even if the purchasers do not directly rely on the misstatements . . . . The causal connection between the defendants' fraud and the plaintiffs' purchase of stock in such a case is no less significant than in a case of direct reliance on misrepresentations.[113]

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101. *Id.* at 227.
102. *Id.*
103. *Id.*
104. *Id.* at 227–28.
105. *Id.* at 228.
106. *Id.*
107. *Id.*
108. *Id.*
109. *Id.* at 242.
110. *Congress, The Supreme Court, and the Rise of Securities-Fraud Class Actions*, *supra* note 97, at 1069.
111. *Id.*
112. *Basic*, 485 U.S. at 250.
113. *Id.* at 241–42 (quoting Peil v. Speiser, 806 F.2d 1154, 1160–61 (3d Cir. 1986)).

The Court, by adopting the fraud-on-the-market theory, created a rebuttable presumption of reliance for an entire class.[114] If a security's price reflects all the publicly available information about the stock, an investor then presumably relies on the price as a proxy of all information that should be available about the security.[115] Although the presumption may be rebutted, this created opportunity for investors to more easily certify as a class when bringing 10b-5 actions.

With the Court's adoption of the fraud-on-the-market theory, *Basic* provided a great benefit to securities plaintiffs.[116] The number of lawsuits based on the fraud-on-the-market theory rose dramatically in response.[117] In fact, such cases tripled in the first three years after *Basic*.[118] After that, the number of cases continued to rise dramatically for the following fifteen years.[119] For example, between 2002 and 2004, over 47% of all federal lawsuits were securities actions.[120] And between 2012 and 2017, the number of securities cases filed increased every year.[121] In 2018 alone, there were 403 securities class action lawsuits filed—the second most in any year.[122] In 2017 there were slightly more, with 412.[123]

V. Curbing Abuse in Class Action Litigation

Along with the increase in the number of securities class actions came an increase in allegations that plaintiffs were abusing the process. The Supreme Court noted Congress's frustration over these alleged abuses in *Merrill Lynch, Pierce, Fenner & Smith, Inc. v. Dabit*, stating:

> While acknowledging that private securities litigation was "an indispensable tool with which defrauded investors can recover their losses," the House Conference Report accompanying what would later be enacted as the Private Securities Litigation Reform Act of 1995 . . . identified ways in which the class-action device was being used to injure "the entire U.S. economy." According to the Report, nuisance filings, targeting of deep-pocket defendants, vexatious discovery requests, and "manipulation by class action lawyers of the

114. Erica P. John Fund, Inc. v. Halliburton, 563 U.S. 804, 810 (2011).

115. *Id.* at 811.

116. Donald C. Langevoort, *Basic at Twenty: Rethinking Fraud on the Market*, 2009 Wis. L. Rev. 151, 179 (2009).

117. *Id.*

118. *Id.*

119. *Id.*

120. John C. Coffee, Jr., *Reforming the Securities Class Action: An Essay on Deterrence and Its Implementation*, 106 Colum. L. Rev., 1534, 1539 tbl.1 (2006).

121. *Congress, The Supreme Court, and the Rise of Securities-Fraud Class Actions*, *supra* note 97, at 1070.

122. Cornerstone Research, Securities Class Action Filings: 2018 Year in Review 5, https://www.cornerstone.com/Publications/Reports/Securities-Class-Action-Filings-2018-Year-in-Review [https://perma.cc/M8U8-V2BM].

123. *Id.*

> clients whom they purportedly represent" had become rampant in recent years . . . . Proponents of the Reform Act argued that these abuses resulted in extortionate settlements, chilled any discussion of issuers' future prospects, and deterred qualified individuals from serving on boards of directors.[124]

A. *The PSLRA and its Unintended Consequences*

To address these abuses, in 1995 Congress enacted the Private Securities Litigation Reform Act ("PSLRA").[125] The PSLRA was designed, at least in part, to heighten the pleading requirements for securities fraud class actions.[126] When enacting the PSLRA, Congress focused on three major areas to reform.[127] First, Congress feared that it was too easy to bring and maintain non-meritorious securities class actions.[128] Some noted that class actions were brought so quickly after drops in the price of securities that there could not have been time to investigate the merits of the claim.[129] Second, because of the defendant's burden in discovery, Congress had concerns that non-meritorious claims settled under coercive conditions.[130] It was cheaper to settle a claim early in the process than to go through the expense of pretrial procedures and discovery.[131] Further, many class actions involve very large monetary exposure, thus increasing the risk associated with a jury trial.[132] Third, Congress feared that the threat of litigation would keep companies from releasing forward-looking statements that are valuable to the investing public.[133] Companies would fear that revealing more information in those statements would create additional fodder for litigation to occur.[134]

To circumvent these fears, Congress made both substantive and procedural changes to the 1933 Act in the PSLRA.[135] Substantively, the PSLRA made four major defendant-friendly changes. First, subject to limited exceptions, it allowed a plaintiff to recover damages only by proving that "the defendant acted with a particular state of mind."[136] To do so, the plaintiffs were required to "state with particularity facts giving rise to a strong inference that the defendant acted

124. *Dabit*, 547 U.S. at 81, (quoting H.R. CONF. REP. No. 104–369, p. 31 (1995)).
125. Private Securities Litigation Reform Act, Pub. L. No. 104-67, 109 Stat. 737 (1995) (codified as amended in scattered sections of 15 U.S.C.).
126. Perino, *supra* note 8, at 294.
127. *Id.* at 290.
128. *Id.*
129. *Id.* at 290–91.
130. *Id.* at 291.
131. *Id.*
132. *Id.*
133. *Id.* at 292.
134. *Id.*
135. *See* Eugene Zelensky, *New Bully on the Class Action Block: Analysis of Restrictions on Securities Class Actions Imposed by the Private Securities Litigation Reform Act of 1995*, 73 NOTRE DAME L. REV. 1135, 1135 (1998).
136. 15 U.S.C. § 78u-4(b)(2)(A) (2012).

with the required state of mind" for each alleged violation of the PSLRA.[137]

Even though this provision was procedural in nature, because it changed the requirements of a complaint, it created new substantive obligations as well.[138] This heightened-pleading requirement required that there be enough circumstantial or direct evidence to support the allegations.[139] The Court in *Tellabs v. Makor Issues & Rights* stated that the strong inference of scienter "must be more than merely plausible or reasonable—it must be cogent and at least as compelling as any opposing inference of nonfraudulent intent."[140]

Another substantive change to federal securities actions in the PSLRA was a provision that extended the safe-harbor protections for forward-looking statements.[141] There are several ways in which a safe harbor may be claimed under the PSLRA. First, if a forward-looking statement is identified as such and "has meaningful cautionary statements identifying important factors that could cause actual results to differ materially from those in the forward-looking statement," then no action may be taken against the maker of the statement.[142] Second, the safe-harbor provision also requires that the forward-looking statement be material to the action being brought.[143] The third hurdle for plaintiffs to circumvent the safe-harbor provision requires that there be "actual knowledge by [a] person that [a] statement was false or misleading" if the statement was made by a natural person.[144] If a business entity released the statement, the plaintiff must show that the statement was made with approval of an executive officer of the business and that the officer had actual knowledge that the statement was false or misleading.[145] In addition, the PSLRA limits when co-defendants would have joint and several liability for securities fraud violations. The PSLRA also contains a provision limiting a plaintiff's recovery. The act limits damages to the difference between the plaintiff's purchase price and the mean purchase price during the ninety-day period after the last disclosure correcting a misstatement or omission.[146]

There is an exception in the statute for those who repurchase securities within the ninety-day period. For securities sold and repurchased within ninety days, the measure of damages is the difference between the sale or purchase price and the mean trading price of the security

137. *Id.*
138. Zelensky, *supra* note 135, at 1136 n.8.
139. Langevoort, *supra* note 116, at 196.
140. Tellabs, Inc. v. Makor Issues & Rights, 551 U.S. 308, 314 (2007).
141. Zelensky, *supra* note 135, at 1136.
142. 15 U.S.C. § 77z-2(c)(1)(A)(i) (2012).
143. *Id.* § 77z-2(c)(1)(A)(ii).
144. *Id.* § 77z-2(c)(1)(B)(i).
145. *Id.* § 77z-2(c)(1)(B)(ii).
146. *Id.* § 78u-4(e)(1).

for a period between the corrective statement and the plaintiff's sale or repurchase of the security.[147] The design of these damage caps is to limit outside market conditions by allowing plaintiffs to recover only for the damages caused by the fraud.[148]

Additionally, under the PSLRA, joint and several liability will be awarded "only if the trier of fact specifically determines that such covered person knowingly committed a violation of the securities laws."[149] Instead, the PSLRA enacted a proportionate liability scheme, in which each defendant would only be responsible for the percentage of damages that each defendant is determined to have caused.[150]

In addition to the requirement that scienter be pled with specificity, there are other important procedural changes. Within twenty days of filing the complaint, there must be notice by publication in a "widely circulated national business-oriented publication or wire service" to inform class members of the pendency of the action and that any class member may petition to become the lead plaintiff.[151] This must be done by the first law firm to file a complaint without any assurance that the firm will become the lead counsel in the lawsuit.[152] This, of course, requires a financial outlay by a law firm with no guarantee of any recovery in the case.

Prior to the PSLRA, courts would usually name the first plaintiff to file as the lead plaintiff in the case.[153] These suits often became quite lucrative for the lead plaintiff.[154] The PSLRA instead created a rebuttable presumption that the lead plaintiff in the action should be the person with the largest financial stake in the outcome of the case.[155] To rebut this presumption, it would have to be shown that the person with the largest stake would not fairly or adequately represent the class or would be subject to defenses that would make them incapable of adequately representing the class.[156] Subject to the approval of the court, the lead plaintiff selects the class counsel.[157]

The PSLRA also limits a person to being the lead plaintiff in only five securities class actions within a three year period.[158] This is titled

147. *Id*. § 78u-4(e)(2).
148. Michael J. Kaufman, *At a Loss: Congress, the Supreme Court and Causation Under the Federal Securities Laws*, 2 N.Y.U. J. L. & Bus. 1, 30–31 (2005).
149. 15 U.S.C. § 78u-4(f)(2)(A) (2012).
150. *Id.* § 78u-4(f)(2)(B).
151. *Id.* § 78u-4(a)(3)(A).
152. Zelensky, *supra* note 135, at 1137.
153. James D. Cox & Randall S. Thomas, *Does the Plaintiff Matter? An Empirical Analysis of Lead Plaintiffs in Securities Class Actions*, 106 Colum. L. Rev. 1587, 1597–98 (2006).
154. *Id.* at 1598.
155. 15 U.S.C. § 78u-4(a)(3)(B) (2012).
156. *Id.* § 78u-4(a)(3)(B)(iii)(II).
157. *Id.* § 78u-4(a)(3)(B)(v).
158. *Id.* § 78u-4(a)(3)(B)(v).

as a restriction on "professional plaintiffs."[159] A professional plaintiff is an individual who holds small interests in many companies.[160] When one of those companies is accused of misdealing, professional plaintiffs become a party to the case, often as the lead plaintiff.[161] By owning shares in the corporations, professional plaintiffs could be exploited because they are interested parties in a class action.[162] Previously, in exchange for their involvement, lead plaintiffs often received extra payment over other class members if a case settled.[163] To eliminate this extra payment to professional plaintiffs, the PSLRA limits the representative plaintiff to the same pro-rata share of the settlement or judgment as other class members.[164]

To increase transparency, the PSLRA discourages putting settlements under seal.[165] A settlement may only be put under seal if it is required to prevent direct harm to one of the parties.[166] The PSLRA also limits attorneys' fees. The fee must be a "reasonable percentage of the amount of any damages and prejudgment interest actually paid to the class."[167] Additionally, the terms of any settlement agreement or proposal must be distributed to the class.[168] This notice must include a statement of the potential outcome of the case, a statement of the attorneys' fees and costs sought in the action, identification and contact information of counsel, and the reason for a proposed settlement.[169]

All of the changes in the PSLRA added an additional layer of restrictions to securities actions brought in federal court.[170] Only limited procedural changes apply in state court securities class actions, although it has not yet been determined which apply.[171] By adding both substantive and procedural requirements to the securities laws, Congress intended to end "strike suits" against issuers of the securities.[172] A "strike suit" is a case in which a person "alleg[es] violations of the

159. *Id.*
160. Zelensky, *supra* note 135, at 1135 n.1.
161. *Id.*
162. *Id.*
163. *Id.*
164. 15 U.S.C. § 78u-4(a)(4) (2012).
165. *Id.* § 78u-4(a)(5).
166. *Id.*
167. *Id.* § 78u-4(a)(6).
168. *Id.* § 78u-4(a)(7).
169. *Id.*
170. Zelensky, *supra* note 135, at 1135. *See also* JAY B. SYKES, CONG. RESEARCH SERV., CLARIFYING "GIBBERISH": SUPREME COURT HOLDS THAT STATE COURTS CAN HEAR SECURITIES ACT LAWSUITS 1–2 (2018), https://fas.org/sgp/crs/misc/LSB10107.pdf [https://perma.cc/8XC7-77Q9].
171. Israel David & Samuel P. Groner, *State Court Securities Lawsuits and the PSLRA in a Post-*'Cyan'*Era*, N.Y. L.J. (May 3, 2018), https://www.friedfrank.com/siteFiles/Publications/NYLJ_Post-Cyan_David_Groner.pdf [https://perma.cc/2NKQ-WMSQ]; *see also* SYKES, *supra* note 170, at 1–2.
172. Lowenthal & Choe, *supra* note 11, at 749.

federal securities laws in the hope that defendants will quickly settle to avoid the expense of litigation."[173] Ending strike suits would lower the costs associated with securities issuance "while maintaining the incentive for bringing meritorious actions."[174]

Congress's intent to end strike suits was not fully realized. This, in large part, was because the PSLRA did not include a provision requiring securities class actions to be litigated in federal courts.[175] This led to the unintended consequence of many plaintiffs choosing to file their cases in state courts to avoid the heightened requirements of the PSLRA.[176] Rule 10b-5 cases were required to be filed in federal courts because the federal courts had exclusive jurisdiction under the 1934 Act.[177] However, many state securities laws provide remedies similar to those available under the 1934 Act, so plaintiffs could avoid federal securities laws altogether.[178] Additionally, the 1933 Act specifically provides concurrent jurisdiction in actions brought under the Act.[179] By not amending the 1933 Act's concurrent jurisdiction provision, the PSLRA did not require that 1933 Act cases be fought in federal court.[180]

Congress noted that prior to passing the PSLRA, there was hardly any significant class action litigation brought in state courts.[181] After its passage, plaintiff attorneys had the incentive to couch what could be federal claims in terms of state claims "where essentially none of the [PSLRA] procedural or substantive protections against abusive suits are available."[182] Additionally, the concurrent jurisdiction of 1933 Act claims further incentivized filing these claims in state courts to avoid the PSLRA. The PSLRA ended up having little effect on Congress's goal of eliminating securities class action strike suits—and the increase in state court litigation was certainly an unintended consequence. Representative Anna Eshoo, when testifying before a Senate subcommittee, noted that if Congress would have thought that there would be a shift from federal to state court litigation, they would have addressed it in PSLRA.[183]

B. *The Effect of State Court Settlements on Parallel Federal Cases*

Shortly after the PSLRA was enacted, the Supreme Court provided further incentive for plaintiffs to bring securities cases in state courts.

173. S. Rep. No. 104-98, at 4 (1995).
174. *Id.*
175. Lowenthal & Choe, *supra* note 11, at 752.
176. *Id.*
177. Michael A. Perino, s*upra* note 8, at 284.
178. O'Connor, *supra* note 48, at 1242.
179. Sykes, *supra* note 170, at 2.
180. *Id.*
181. H.R. Rep. 105-640, at 10 (1998).
182. *Id.*
183. Lowenthal & Choe, *supra* note 11, at 752.

In 1996, the Court decided *Matsushita Electric Industrial Company v. Epstein*.[184] *Matsushita* involved a tender offer in which Matsushita Electric Industrial Company ("Matsushita") acquired MCA.[185] Two separate class action lawsuits were filed. One case was filed in a Delaware state court claiming only that MCA violated state law by breaching its fiduciary duties for not maximizing shareholder value.[186] Matsushita was added to the complaint on allegations that it conspired with MCA to violate these laws.[187] The second case was filed in a California federal district court, alleging that Matsushita violated the 1934 Act in its tender offer.[188] The parties reached a global settlement in the Delaware state action, releasing all claims related to the Matsushita–MCA acquisition.[189] At issue in the Court was Matsushita's claim that the Full Faith and Credit Act[190] barred the federal class from proceeding because its claims were settled as part of the Delaware settlement.[191] The plaintiffs in the federal class action disagreed, noting that 1934 Act allegations were within the sole jurisdiction of the federal courts.[192] Therefore, the plaintiffs reasoned the Delaware settlement could not be used as a vehicle to settle federal claims.[193] The Court ruled that acceptance of the settlement by the Delaware state court would have a preclusive effect on the settlement, including the 1934 Act claims, "notwithstanding the fact that respondents could not have pressed their [1934 Act] claims in the [Delaware state court]."[194]

In addition to avoiding the heightened requirements of the PSLRA, the holding in *Matsushita* provided an additional incentive to file in state court because if an action was brought in state court, under state court claims, the federal claims (including those under Rule 10b-5) could be settled in the state action.[195] *Matsushita* allowed a plaintiff to find a plaintiff-friendly state court in which the class could receive a global settlement of both the federal and state claims.[196] These settlements are often "sweetheart deals" where counsel receive sizable attorneys' fees while leaving the class plaintiffs less than what they expected to receive in a separate court action.[197] The combination of

184. Matsushita v. Epstein, 516 U.S. 367 (1996).
185. *Id.* at 369–70.
186. *Id.* at 370.
187. *Id.*
188. *Id.*
189. *Id.* at 371.
190. 28 U.S.C. § 1738 (2012).
191. *Matsushita*, 516 U.S. at 372.
192. *Id.* at 380.
193. *Id.* at 372.
194. *Id.* at 378.
195. Perino, s*upra* note 8, at 310–11.
196. *Id.* at 311.
197. Edward F. Sherman, *Class Action Fairness Act and the Federalization of Class Actions*, 238 F.R.D. 321, 344 n.138 (2007).

the PSLRA and *Matsushita* led to a dramatic rise in the number of cases brought in state courts.[198]

C. *The SLUSA Loopholes*

Congress, soon after realizing that the PSLRA caused a spike in state securities class action litigation, took action by enacting the Securities Litigation Uniform Standards Act of 1998 ("SLUSA").[199] Congress decided that the provisions in the 1933 Act that allowed for concurrent state and federal jurisdiction, coupled with its anti-removal provisions, prevented the PSLRA from accomplishing its goals.[200] In the introduction to SLUSA, Congress specifically found:

> [I]n order to prevent certain State private securities class action lawsuits alleging fraud from being used to frustrate the objectives of the [PSLRA], it is appropriate to enact national standards for securities class action lawsuits involving nationally traded securities, while preserving the appropriate enforcement powers of State securities regulators and not changing the current treatment of individual lawsuits.[201]

SLUSA was designed to create a balance between state and federal class actions. Claims that only impacted one state were to be left to that state's courts. Claims of national importance would no longer circumvent the heightened requirements of the PSLRA; SLUSA eliminated state court jurisdiction over these class actions.[202] They did so primarily in section 16(b) of the Act, which states in relevant part:

> No covered class action based upon the statutory or common law of any State or subdivision thereof may be maintained in any State or Federal court by any private party alleging—
> (1) an untrue statement or omission of a material fact in connection with the purchase or sale of a covered security; or
> (2) that the defendant used or employed any manipulative or deceptive device or contrivance in connection with the purchase or sale of a covered security.[203]

SLUSA broadly defined the terms "covered class action" and "covered security." A "covered class action" is one in which damages are sought for fifty or more people or prospective class members.[204] A "covered security" is one that is traded on a national exchange.[205] SLUSA also amended the anti-removal provision of the 1933 Act. It

198. Lowenthal & Choe, *supra* note 11, at 752.
199. Securities Litigation Uniform Standards Act of 1998, Pub. L. No 105-353, 112 Stat. 3227 (1998) (codified in scattered sections of 15 U.S.C.).
200. O'Connor, *supra* note 48, at 1243.
201. Securities Litigation Uniform Standards Act § 2(5).
202. Greene et al., *supra* note 4, at 2.
203. This section was later codified as 15 U.S.C. § 77p(b).
204. 15 U.S.C. § 78bb(f)(5)(B) (2011).
205. *Id.* § 77r(b) (2015).

stated that any "covered class action brought in any state court involving a covered security . . . shall be removable to the Federal district court in which the action is pending."[206] Additionally, it limited the concurrent jurisdiction of federal and state courts provided in the 1933 Act. SLUSA allows for concurrent jurisdiction "except . . . with respect to covered class actions."[207]

Eliminating the anti-removal provisions and concurrent jurisdiction had the effect of preempting class action litigation of covered securities that are based on state law.[208] This preemption led to covered class actions being primarily litigated on claims under federal legislation (the 1933 Act and the 1934 Act).[209] Therefore, removing a class action brought under state law involving a covered security to federal court effectively dismissed the state law claims.[210] Congress enacted SLUSA in part because national securities issuers were potentially subject to a patchwork of the legislative will of each of the states.[211] The dismissal of state court actions, upon removal, prevents state courts from deciding not to enforce the removal provisions of SLUSA.[212] Thus, SLUSA ended much of the forum shopping that led cases to be filed in states that were seen as plaintiff-friendly.[213]

However, like the PSLRA, SLUSA had unintended consequences after its enactment. In its attempt to balance the state and federal actions, Congress left many avenues open for a state court to hear securities cases. For example, SLUSA specifically excluded actions that were brought against state and local pension funds.[214] It was also theorized that because SLUSA only pertained to covered securities, actions brought concerning securities not traded on a national exchange could still be litigated under state laws.[215] Congress likely intended these provisions to allow for these types of cases to still be brought in state courts. What Congress did *not* address became more important—and led to SLUSA's own unintended consequences. SLUSA left what has been described as a loophole, which allowed some plaintiffs to still litigate securities class actions in state courts.[216]

206. *Id.* § 77p(c) (2018).

207. *Id.* § 77v(a) (2018).

208. O'Brien, *supra* note 13, at 861–62.

209. *Id.* at 862.

210. Kircher v. Putnam Funds Tr., 547 U.S. 633, 644 (2006).

211. Lowenthal & Choe, *supra* note 11, at 757.

212. Cyan, Inc. v. Beaver Cty. Emps. Ret. Fund, 138 S. Ct. 1061, 1068 (2018).

213. *See id.*

214. 15 U.S.C. § 77p(2)(A) (2018).

215. *Kircher*, 547 U.S. at 636 n.1.

216. *See, e.g.*, J. Tyler Butts, *Removal of Covered Class Actions Under SLUSA: The Failure of Plain Meaning and Legislative Intent as Interpretive Devices, and the Supreme Court's Decisive Solution*, 1 WM. & MARY BUS. L. REV. 169, 187 (2010); Cook *supra* note 17, at 168.

SLUSA did not in itself displace state law with federal law.[217] This led to questions of how the removal provision should be applied. SLUSA's removal provision, described in section 16(c) of the act,[218] reads:

> Any covered class action brought in any State court involving a covered security, as set forth in subsection (b), shall be removable to the Federal district court for the district in which the action is pending, and shall be subject to subsection (b).[219]

By referring to section 16(b) of SLUSA, the removal provision in section 16(c) facially only applies to actions "based upon the statutory or common law of any State."[220] By its terms, therefore, SLUSA does not impact claims based upon federal law. The 1934 Act, however, does require that cases brought under it be filed in federal court.[221] However, SLUSA does not address the concurrent jurisdiction and anti-removal provisions in section 22(a) of the 1933 Act.[222] The loophole in SLUSA's jurisdictional provisions led to the controversial result that claims based on state laws that allege misrepresentation or omission of material fact may be litigated only in federal court; however, federal claims under the 1933 Act may be litigated in state courts in some jurisdictions.[223]

By not addressing the anti-removal and concurrent jurisdiction clauses of the 1933 Act, SLUSA led to a split in interpretation by federal district courts. In a rare occurrence, this split in district courts did not have any appellate circuit court opinions to interpret them.[224] These district court cases typically involved a question of remand when a case had been removed to federal court.[225] Because remand orders cannot be appealed,[226] there "likely never will be" any circuit court decisions.[227] District courts in the First and Seventh Circuits generally supported a narrow interpretation of SLUSA's anti-removal provision.[228] These courts interpreted the language in section 16(b) of

217. *Id.*

218. 15 U.S.C. § 77p(c) (2018).

219. *Id.*

220. *Id.* § 77p(b).

221. 15 U.S.C. § 78aa(a) (2018).

222. 15 U.S.C. § 77v(a) (2018).

223. O'Brien, *supra* note 13, at 863.

224. Jennifer Johnson, *Securities Class Actions in State Court*, 80 U. CIN. L. REV. 349, 360 (2012).

225. *See id.*

226. 28 U.S.C § 1447(d) (2018).

227. Brief of Amici Curiae Law Professors in Support of Petitioners at 3, Cyan, Inc. v. Beaver Cty. Emps. Ret. Fund, 138 S. Ct. 1061 (2018) (No. 15-1439) [hereinafter Brief of Law Professors].

228. Butts, *supra* note 216, at 175–76.

SLUSA to be specific as to where removal was allowed.[229] This more narrow interpretation allowed for 1933 Act fraud claims to be litigated in state courts without the ability to be removed.

District courts in the Third, Fourth, and Sixth Circuits approached SLUSA's anti-removal provision differently. They applied a broad interpretation based on congressional intent.[230] These courts reasoned that it was Congress's intent under SLUSA to have all covered securities class action cases litigated in the federal courts.[231]

The Second, Fifth, and Ninth Circuits' district courts were inconsistent in how they interpreted SLUSA's removal provision. Sometimes they would interpret the statute broadly, and sometimes narrowly.[232] There were times within months where the same district would interpret the statute in opposite ways.[233]

The Supreme Court, in *Kircher v. Putnam Funds Trust* touched on the removal issue.[234] *Kircher*, however, focused on whether an order remanding a case removed under SLUSA was appealable.[235] The Court held that those remands were not.[236] In its discussion, the Court noted that there was "no reason to reject the straightforward reading: removal and jurisdiction to deal with removed cases is limited to those precluded by the terms of subsection (b)."[237] Under this interpretation, removal to federal court would be unavailable only for state law claims in connection with the purchase or sale of securities.[238] The Court further stated "[i]f the action is not precluded [under subsection (b)], the federal court likewise has no jurisdiction to touch the case on the merits, and the proper course is to remand to the state court . . . ."[239] *Kircher* did not involve any alleged violations of the 1933 Act.[240] Instead, it involved claims only under state law.[241] As such, this part of *Kircher* is often deemed to be *dicta*, and is not considered mandatory authority in many subsequent cases examining the remov-

229. *Id. See also* Nauheim v. Interpublic Grp. of Cos., No. 02-C-9211, 2003 WL 1888843 (N.D. Ill. Apr. 16, 2003); In re Tyco Int'l, Ltd., 322 F. Supp. 2d 116 (D.N.H. 2004).

230. Butts, *supra* note 216, at 176. *See also* Lowinger v. Johnston, No. 05-316-H, 2005 WL 2592229 (W.D.N.C. Oct. 13, 2005); In re King Pharmaceuticals, Inc., 230 F.R.D. 503, 505 (E.D. Tenn. 2004); Pinto v. Vonage Holdings Corp., No. 07-0062, 2007 WL 1381746 (D.N.J. May 7, 2007).

231. Butts, *supra* note 216, at 176–78.

232. *Id.* at 178.

233. Johnson, *supra* note 224, at 360.

234. Kircher v. Putnam Funds Tr., 547 U.S. 633 (2006).

235. *Id.* at 635–36.

236. *Id.* at 636.

237. *Id.* at 643.

238. Lowenthal & Choe, *supra* note 11, at 774.

239. *Kircher*, 547 U.S. at 644.

240. O'Connor, *supra* note 48, at 1247–48.

241. *Id.*

ability of 1933 Act claims.[242] Therefore, *Kircher* did little to close the split in the courts regarding SLUSA's removal provision.

D. *CAFA Exclusions*

In 2005, Congress enacted the Class Action Fairness Act of 2005 ("CAFA").[243] CAFA was directed at perceived abuses in class actions in general.[244] Congress noted that there had been a "flood" of state court class actions in "improbable locations."[245] Further, Congress noted that in the decade prior to CAFA's adoption, there had been many abuses in class actions that harmed both legitimate class action claims and interstate commerce.[246] For example, Congress recognized that class members often received little or no benefit while their counsel were awarded large fees.[247] Congress intended to expand federal jurisdiction over class action lawsuits to remedy these abuses,[248] serving Congress's purpose of addressing class action cases of national importance in federal courts.[249] CAFA accomplished this by giving federal district courts original jurisdiction over class actions where the amount in controversy is over $5 million, there are more than 100 plaintiffs, and there is minimal diversity of the parties.[250]

While addressing class action lawsuits generally, Congress specifically excluded securities class actions from CAFA's provisions. CAFA states that its provision giving original jurisdiction in federal courts:

> shall not apply to any class action that solely involves a claim—
> (A) concerning a covered security as defined under . . . the Securities Act of 1933 . . . and . . . of the Securities Exchange Act of 1934 . . . ;
> (B) that relates to the internal affairs or governance of a corporation or other form of business enterprise and that arises under or by virtue of the laws of the State in which such corporation or business enterprise is incorporated or organized; or
> (C) that relates to the rights, duties (including fiduciary duties), and obligations relating to or created by or pursuant to any security (as

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242. Butts, *supra* note 216, at 194.

243. Class Action Fairness Act (CAFA), Pub. L. No. 109-2, 119 Stat. 4 (2005) (codified in scattered sections of 28 U.S.C.).

244. Patricia Hatamyar Moore, *Confronting the Myth of* "*State Court Class Action Abuses*" *Through an Understanding of Heuristics and a Plea for More Statistics*, 82 UMKC L. REV. 133, 134 (2013).

245. S. REP. NO. 109-14, at 13–14. It should be noted that there is a question as to whether there was adequate information to make those determinations, and therefore the assertion of a flood of state class actions made be exaggerated. *See, e.g.*, Moore, *supra* note 244.

246. CAFA § 2(a)(2).

247. *Id.* § 2(a)(3).

248. Cook, *supra* note 17, at 622.

249. CAFA § 2(b)(2).

250. 28 U.S.C. § 1332(d)(2), (d)(5) (2012). Minimal diversity only requires that any plaintiff who is a class member must be from a jurisdiction other than any defendant. *Id.*

defined under section 2(a)(1) of the Securities Act of 1933 . . . and the regulations issued thereunder).[251]

Congress reasoned that the securities exemptions were included in CAFA "to avoid disturbing in any way the federal vs. state court jurisdictional lines already drawn in the securities litigation class action context by the enactment of [SLUSA]."[252]

E. *1933 Act Claims in State Court After CAFA*

Because CAFA did not seek "to disturb the carefully crafted framework" of jurisdiction over securities claims established in SLUSA, the issues left unaddressed in SLUSA had a distinct impact on the litigation landscape.[253] In the decades since SLUSA's enactment, there have been dozens of state court class actions litigated under 1933 Act claims.[254] The number of class action cases filed in state courts under the 1933 Act indicated that forum shopping was a viable option.[255] Because CAFA reduced the ability to forum shop in class actions, it seemed curious to some that securities cases were specifically excluded.[256] The split involved some district courts finding that SLUSA granted exclusive federal jurisdiction over covered class actions that allege only claims under the 1933 Act.[257] Others held the plain language of the 1933 Act would not allow for removal of claims that were brought in state courts.[258]

Forum shopping led to plaintiffs filing 1933 Act cases in courts where they were not likely to be removed. California, particularly in the Northern District, and New York, particularly in the Southern District, handle most of the securities cases in the United States.[259] Between 2011 and 2015, federal district courts dismissed 29% of cases that were filed with only 1933 Act claims.[260] In contrast, during this same period, California state courts only dismissed 8% of these cases without leave to amend.[261] Since California federal district courts generally allowed 1933 Act class actions to proceed in state court, California state courts saw a great increase in the amount of cases brought there. In 2010, California state courts only had one new 1933 Act class action filed.[262] These numbers increased dramatically in subsequent years: 2015 saw fifteen cases, 2016 saw nineteen, 2017 saw seven, and

251. 28 U.S.C. § 1332(d)(9) (2012).
252. S. Rep. No. 109-14, at 45 (2005).
253. *Id.* at 50.
254. Brief of Law Professors, *supra* note 227, at 3.
255. Cook, *supra* note 17, at 622.
256. *Id.*
257. Brief of Law Professors, *supra* note 227, at 1.
258. *Id.* at 6 n.10, 7.
259. *Id.* at 8.
260. *Id.* at 3.
261. *Id.*
262. Cornerstone Research, *supra* note 122, at 19.

2018 saw sixteen.[263] Thus, CAFA did little to quell securities class actions being brought in state courts.

VI. *Cyan* Confirms that 1933 Act Claims May Be Brought in State Courts

In 2018, the Supreme Court's *Cyan* decision resolved part of the competing opinions of the federal district courts regarding jurisdiction of class actions brought under the 1933 Act.[264] The petitioners in *Cyan* were the officers and directors of Cyan, Inc. ("Cyan"), a telecommunications company.[265] The respondents were a group consisting of one individual investor and three pension funds ("Investors").[266] The Investors had purchased Cyan stock during an initial public offering.[267] After the stock declined in value, the investors initiated a class action against Cyan in California Superior Court.[268] The complaint alleged that Cyan's offering documents contained material misstatements.[269] These claims were made solely as violations of the 1933 Act and did not contain any alleged violations of state law.[270] Cyan moved to dismiss the lawsuit alleging that state courts lacked subject matter jurisdiction to hear 1933 Act claims.[271] The California Superior Court denied the motion to dismiss, and the California appellate courts declined to review the ruling.[272]

Cyan based its dismissal motion on an interpretation of SLUSA amendments to the concurrent jurisdiction section of the 1933 Act that is now codified as 15 U.S.C. § 77v(a).[273] Essentially, Cyan claimed that this statute, as amended, stripped state courts of the power to adjudicate state law claims that involved covered class actions under the SLUSA definition.[274] To resolve a split among the federal and state courts regarding state court jurisdiction of 1933 Act class actions, the United States Supreme Court granted *certiorari*.[275]

Cyan claimed that state courts lacked jurisdiction, arguing that the legislative history and purpose behind SLUSA's enactment prohibited it.[276] Cyan argued that SLUSA was put in place to make good on the promise of the PSLRA heightened pleading requirements by requir-

263. *Id.*
264. Cyan, Inc. v. Beaver Cty. Emps. Ret. Fund, 138 S. Ct. 1061 (2018).
265. *Id.* at 1068.
266. *Id.*
267. *Id.*
268. *Id.*
269. *Id.*
270. *Id.*
271. *Id.*
272. *Id.*
273. *Id.*
274. *Id.*
275. *Id.* at 1068–69.
276. *Id.* at 1072.

ing that 1933 Act class actions be brought solely in federal courts.[277] Cyan cited a legislative report that indicated that SLUSA was conceived "to prevent plaintiffs from seeking to evade the protections [the PSLRA] provides against abusive litigation by filing suit in State, rather than in Federal, court."[278]

The Court instead focused on the interpretation of the statute itself. The Court's primary focus was on a clause in section 77v(a) that reads:

> The district courts of the United States . . . shall have jurisdiction[,] concurrent with State and Territorial courts, *except as provided in section 77p of this title with respect to covered class actions*, of all suits in equity and actions at law brought to enforce any liability or duty created by this subchapter.[279]

The italicized part of the statute was referred to by the Court as section 77v(a)'s "except clause."[280] Cyan debated over how to reconcile the except clause with section 77(p), the statute referred to in the clause. Cyan argued that the clause only referred to the covered class actions that are defined in section 77p(f)(2).[281] Cyan maintained that there were "two halves" to the except clause, the first was to point the reader in the direction of where to look (section 77p).[282] The except clause's second part then gave effect to the words "covered class action."[283] If the section referred to covered class actions, then the except clause would remove concurrent jurisdiction to all claims, whether based on federal or state law.

The Investors argued that the except clause was only a conforming amendment.[284] It therefore should be read as aligning the jurisdictional provisions of section 77v(a) with the provisions of section 77p that preclude state law claims from being litigated in state courts.[285] This would leave other cases, such as those filed with only 1933 Act claims, unaffected.[286] Cyan responded that if this were the interpretation, then the except clause would "serve no purpose at all."[287]

The Court, when examining the except clause, experienced difficulty interpreting the interplay between sections 77v(a) and 77p. During oral argument Justice Alito noted:

> Our late colleague [Justice Scalia] wrote a book called Reading Law, which provides guidance about how you read statutes. And I

277. *Id.*
278. *Id.* (quoting H.R. CONF. REP. NO. 105–803, at 13 (1998)). *Cyan* also referred to other legislative reports with similar language. *Id.* at 1072.
279. *Id.* at 1068 (quoting 15 U.S.C. § 77v(a)) (emphasis added).
280. *Id.*
281. *Id.* at 1070.
282. Transcript of Oral Argument, *supra* note 15, at 10.
283. *Id.*
284. *Id.* at 51.
285. *Id.*
286. *Id.*
287. Cyan, Inc. v. Beaver Cty. Emps. Ret. Fund, 138 S. Ct. 1061, 1073 (2018).

> looked through that to see what we are supposed to do when Congress writes gibberish. And that's what we have here. You said it's obtuse. That's flattering. And we have very smart lawyers here who have come up with creative interpretations, but this is gibberish. It's . . . just gibberish.[288]

When the Investors' attorney tried to clarify their interpretation of the except clause, Justice Gorsuch responded with: "[A]ren't we stuck with gibberish your way too? I mean, it seems like it's gibberish all the way down here . . . ."[289] After much frustration, Justice Gorsuch later stated that the Court had to try to give effect to Congress's language, opining that "respect for the legislative process dictates that we afford some meaning to these words."[290]

When giving meaning to the words of section 77v(a), the unanimous Court ruled that the except clause modified all of section 77p.[291] In addressing Cyan's argument that it only modified covered class actions, the Court stated that it would be "cherry pick[ing] from the material covered by the statutory cross-reference."[292] If Congress wanted the except clause to refer only to section 77p(f)(2), it presumably would have done so by adding that subsection into the statute when it was created.[293] By its interpretation of the except clause, the Court ruled that under SLUSA "state court jurisdiction over 1933 Act claims . . . continues undisturbed."[294]

A. *The Impact of* Cyan

Cyan had an immediate impact on the filing of new 1933 Act class action claims in state courts. Prior to SLUSA, judges in the Southern District of New York generally ruled that federal courts had exclusive jurisdiction over 1933 Act class actions.[295] Accordingly, New York saw a dearth of 1933 Act cases filed in state courts in the eight years prior to *Cyan's* ruling in 2018.[296] After *Cyan* clarified that there was concurrent jurisdiction over 1933 Act claims, the number of 1933 Act class actions increased significantly.[297] New York state courts saw thirteen new 1933 Act cases filed, where it had none the year before.[298] All thirteen were filed after the *Cyan* decision.[299] This flurry of new cases suggests that forum shopping 1933 Act cases in state courts is alive

288. Transcript of Oral Argument, *supra* note 15, at 11.
289. *Id.* at 47.
290. *Id.* at 48.
291. *Cyan*, 138 S. Ct. at 1063–64.
292. *Id.* at 1070.
293. *Id.*
294. *Id.* at 1069.
295. Brief of Law Professors, *supra* note 227, at 8.
296. Cornerstone Research, *supra* note 122, at 19.
297. *Cyan*, 138 S. Ct. 1063.
298. Cornerstone Research, *supra* note 122, at 19.
299. *Id.*

and well. This trend is likely to continue, with the probable result that some states will emerge as plaintiff-friendly. These states will then start receiving a greater portion of the new claims.

B. *Does* Cyan *Leave a Loophole for Non-Covered Securities?*

Another loophole not addressed in *Cyan* was the impact of CAFA on 1933 Act claims. Because the securities in question in *Cyan* were covered securities, they met CAFA's securities exemption, so *Cyan* did not discuss CAFA.[300] Currently there is a split in the federal circuit courts about how to interpret the CAFA removal provision's impact on non-covered securities.[301] These securities do not meet any of the three exemptions articulated in CAFA.[302] Rather, these cases address two apparently competing statutes. Section 22(a) of the 1933 Act generally forbids removal of covered securities cases to federal court.[303] CAFA, on the other hand, requires removal of most class actions within its coverage to federal court.

There are some types of class actions in which CAFA forbids removal. The first is the "local controversy exemption."[304] Under this exception, removal must be declined over a class action where two-thirds of the plaintiffs and at least one of the defendants are from the same state and that state is where the principal injuries occurred.[305] Significant relief must be sought from that defendant because of his or her conduct, so long as no similar class action was filed against any of the same defendants within the past three years.[306] There is also a "home state controversy exemption."[307] This precludes removal when "two-thirds or more of the members of all proposed plaintiff classes in the aggregate, and the primary defendants, are citizens of the State in which the action was originally filed."[308] Additionally, federal courts have discretion to decline jurisdiction over cases in which between one-third and two-thirds of the plaintiffs and the defendants are citi-

300. Philip C. Babler, *SCOTUS Keeps Door Open for Federal-Law, State-Court Securities Class Actions. Where Does This Leave* Katz?, FOLEY (Sept. 28, 2018), https://1npdf11.onenorth.com/pdfrenderer.svc/v1/abcpdf11/GetRenderedPdfByUrl/SCOTUS%20Keeps%20Door%20Open%20for%20FederalLaw%20StateCourt%20S.pdf/?url=https%3a%2f%2fwww.foley.com%2fen%2finsights%2fpublications%2f2018%2f09%2fscotus-keeps-door-open-for-federallaw-statecourt-s?format=pdf&attachment=false [https://perma.cc/LEM4-TXU6].

301. Johnson, *supra* note 224, at 359–60.

302. *See* 28 U.S.C. § 1332(d)(9) (2012).

303. 15 U.S.C § 77v(a) (2012).

304. Johnson, *supra* note 224, at 357.

305. 28 U.S.C. § 1332(d)(4)(A) (2012).

306. *Id.*

307. Johnson, *supra* note 224, at 357.

308. 28 U.S.C. § 1332(d)(4)(B) (2012).

zens of the same state.[309] If a security does not meet one of the exemptions under CAFA, it is removable to federal court.[310]

The conflict over whether CAFA removal would trump the non-removal provision of SLUSA was realized in the Ninth Circuit in *Luther v. Countrywide Home Loans Servicing*.[311] In *Luther*, the plaintiffs initiated a class action alleging only violations of the 1933 Act.[312] They alleged that the defendants violated sections 11, 12(a)(2), and 15 of the 1933 Act by issuing false and misleading registration statements and prospectus documents for some mortgage pass-through certificates. The parties agreed that the pass-through certificates were not covered securities as defined by SLUSA.[313] The defendants removed the case to federal court using CAFA.[314] Once in federal court, the plaintiffs then tried to remand the case back to state court stating that section 22(a) of the 1933 Act prohibited removal.[315] In deciding the case, the Ninth Circuit stated "[i]t is a basic principle of statutory construction that a statute dealing with a narrow, precise, and specific subject is not submerged by a later enacted statute covering a more generalized spectrum."[316] Using this maxim of statutory construction, the court noted that section 22(a) of the 1933 Act was the more specific statute, arising only for securities claims.[317] CAFA applied to class actions in general.[318] As such, the Ninth Circuit applied section 22(a) and not CAFA, and therefore remanded the case back to state court.[319] After *Luther*, almost all California federal courts have remanded 1933 Act cases to state court.[320] This appears to have led, at least in part, to the increase of 1933 Act claim California class actions because the increase happened soon after *Luther*.[321]

The Seventh Circuit came to the opposite conclusion in *Katz v. Gerardi*.[322] At issue in *Katz* were securities of a real investment trust that

309. *Id.* § 1332(d)(3).

310. *Id.* § 1332(d)(11)(A). There are other limited exemptions, but they would likely not affect private securities litigation. *See* Johnson, *supra* note 224, at 360.

311. Luther v. Countrywide Home Loans Servicing, 533 F.3d 1031, 1032 (9th Cir. 2008).

312. *Id.* at 1032–33.

313. *Id.* at 1033 n.1.

314. *Id.* at 1033.

315. *Id.*

316. *Id.* at 1034 (quoting Radzanower v. Touche Ross & Co., 426 U.S. 148, 153 (1976)).

317. *Id.*

318. *Id.*

319. *Id.*

320. Michael W. Stocker & Francis P. McConville, *Securities Act Cases Are Surging. . .in State Courts?*, L.A. DAILY J. (July 28, 2015), https://info.labaton.com/hubfs/Daily-Journal-Stocker-McConville.pdf?t=1542747634819 [https://perma.cc/VY9P-TK3Q].

321. *See supra* text accompanying notes 259–63.

322. Katz v. Gerardi, 552 F.3d 558, 563 (7th Cir. 2009).

were exchanged for some real property.[323] After a merger, holdings in those securities were transferred to a different security with allegedly less tax benefits.[324] The plaintiffs alleged that this transfer violated the terms of the original security.[325] As in *Luther*, these securities were not covered securities as defined in SLUSA.[326] The plaintiffs filed a state law class action in Illinois.[327] The defendants then used CAFA to remove the case to federal court.[328] The Northern District of Illinois, citing *Luther*, remanded the case back to state court stating that section 22(a) prohibited the removal because it was more specific than CAFA.[329] The Seventh Circuit, in reviewing the remand decision, specifically disagreed with the holding in *Luther*.[330] The court opined that the statutory maxim used to decide *Luther* did not apply. It reasoned that a specific statute impacted by a newer but more general one only controls the newer one when one of the statutes is a subset of the other.[331] The Seventh Circuit held that section 22(a) is not a subset of CAFA, noting:

> Is the 1933 Act more specific because it deals only with securities law, or is [CAFA] more specific because it deals only with nationwide class actions? There is no answer to such a question, which means that the canon favoring the specific law over the general one won't solve our problem.[332]

The court, by opining that the maxim did not apply, ruled that the case was removable under CAFA.[333] Opposite to the Ninth Circuit in *Luther*, the Seventh Circuit allowed CAFA to trump section 22(a).

The Seventh Circuit again allowed for removal of claims for non-covered securities in *Appert v. Morgan Stanley Dean Witter, Inc.*[334] *Appert* involved a fee dispute on the purchase of some securities.[335] In dispute over a misrepresentation, the Northern District of Illinois found that the misrepresentation was not material, and dismissed the case.[336] On appeal, the Seventh Circuit found that the defendant had met its jurisdictional burden to bring the case under CAFA.[337] It was incumbent on the plaintiff to prove that the securities would be ex-

323. *Id.* at 559.
324. *Id.*
325. *Id.*
326. *Id.* at 562–63.
327. *See id.* at 559.
328. *Id.*
329. Katz v. Gerardi, No. 08 cv 04035, 2008 WL 4376815, at *4 (N.D. Ill. Sept. 23, 2008).
330. *Katz*, 552 F.3d at 562.
331. *Id.* at 561.
332. *Id.* at 561–62.
333. *Id.* at 562.
334. Appert v. Morgan Stanley Dean Witter, Inc., 673 F.3d. 609, 619 (7th Cir. 2012).
335. *Id.* at 613.
336. *Id.*
337. *Id.* at 617.

empted because of CAFA's securities exemptions.[338] The plaintiff could not, and as such, the court ruled that CAFA required removal to federal court.[339]

A New York federal district court also disagreed with the rationale espoused by the Ninth Circuit. In *New Jersey Carpenters Vacation Fund v. Harborview Mortgage Loan Trust*, a class action over the prospectus for the issuance of bonds also raised the question of removal.[340] The plaintiffs brought claims under the 1933 Act and the defendant removed the case to federal court based on CAFA. The plaintiffs then tried to remand the case back to state court.[341] The court found that the bonds did not meet any exceptions laid out in CAFA. The court ruled against the remand stating that CAFA "creates original jurisdiction for and removability of *all* class actions that meet the minimal requirements and do not fall under one of the limited exceptions."[342] The court, in its denial of the motion, noted that there was a split in the circuits and that CAFA should overrule section 22(a) because this interpretation "comports more closely with the decisions in this [the Second] Circuit."[343]

The split in the Seventh and Ninth Circuits as to whether CAFA trumps section 22(a) provides yet another avenue for forum shopping. It further appears that in *New Jersey Carpenters Vacation Fund*, courts in the Second Circuit also disagree with the Ninth Circuit approach, adopting that of the Seventh Circuit. This creates another split between the two jurisdictions with the most securities cases, California and New York. If a plaintiff initiates a class action, he or she may prefer to bring it in a state that appears to oppose removal so the case will remain in state court. If neither Congress nor the Supreme Court address the issue, other circuits may also opine on the issue, broadening the options for plaintiff forum shopping. Other legal scholars note this irony, stating that "plaintiffs will use forum-shopping to avoid a statute [CAFA] whose very purpose was to prevent plaintiffs from forum-shopping."[344]

VII. Conclusion

There has been a long history of plaintiffs attempting to bring securities class actions in state courts, especially those seen as plaintiff-

338. *Id.* at 619.

339. *See id.* at 621–22.

340. N.J. Carpenters Vacation Fund v. HarborView Mortg. Loan Tr. 2006-4, 581 F. Supp. 2d 581, 582 (S.D.N.Y. 2008).

341. *Id.*

342. *Id.* at 584 (emphasis supplied).

343. *Id.* at 582.

344. James E. Brandt & Eric S. Olney, *Removal of Class Action Securities Cases in the Age of CAFA*, Bloomberg L. Reports (2009), https://www.lw.com/thoughtLeadership/removal-class-action-securities-cases-in-age-of-cafa [https://perma.cc/9UCT-UUQ3].

friendly. *Cyan* has affirmed that this type of forum shopping is still available in 1933 Act cases involving covered securities. This option exists even after Congress enacted the PSLRA and SLUSA to address securities class actions specifically. The PSLRA was ineffective because it had the unintended consequence of pushing cases to state courts. SLUSA, which was designed to force securities class action litigation to take place in federal court, left a loophole for 1933 Act claims. This is because Congress, when drafting SLUSA, was unclear enough that Justice Alito called its removal provision gibberish. In addition to the PSLRA and SLUSA, which only affected securities class actions, Congress also created CAFA. CAFA was enacted to require the litigation of all class actions of national importance in federal courts. However, the securities exemptions in CAFA allowed for another loophole. It caused a split in the circuits as to whether 1933 Act class action claims over non-covered securities are exempted from CAFA. This now allows another avenue for forum shopping.

In *Cyan*, the Court showed its reluctance to use legislative history and intent to determine jurisdictional requirements under SLUSA. The Court resolved *Cyan* primarily using statutory interpretation, even though the statute was unclearly written. This indicates that the Court believes that any attempts at clarifying are purely in the purview of Congress.

It is unclear how courts will interpret CAFA's impact on the 1933 Act's concurrent jurisdiction and anti-removal provisions in class actions involving non-covered securities. Certainly, the Supreme Court could close the split in the circuits. If it were to adopt the Ninth Circuit interpretation, then class actions over covered and non-covered securities could both take place in state courts. If it adopted the Seventh Circuit interpretation, then class actions involving covered securities could take place in state courts, but those involving non-covered securities would have to be brought in federal courts. Either way, *Cyan* would still allow some avenues for forum shopping.

Congress could easily remedy these loopholes by creating clear statutes that would put all securities class actions of national importance in federal court. This would meet the stated goals of the PSLRA, SLUSA, and CAFA. It could close the loophole that SLUSA created allowing 1933 Act claims to be litigated in state courts by following the Court's recommendation in *Cyan*. Congress could add an amendment to SLUSA specifying that the exemptions referred to in section 77v apply to section 77p(f)(2) instead of section 77p in its entirety. Alternatively, CAFA could be amended to clarify that it does require removal of cases over non-covered securities to federal court. If Congress chooses either option, then 1933 Act cases of national importance would have to be litigated in federal court. This would meet the stated goals of the PSLRA, SLUSA, and CAFA.