

Supreme Court: Unanimously Upholds State Court Jurisdiction Over Class Actions Alleging Only Claims Under the Securities Act of 1933

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On March 20, 2018, the Supreme Court unanimously held that state courts have jurisdiction over class actions alleging only violations of the Securities Act of 1933 (“the ‘33 Act”).^[1] *Cyan v. Beaver Cty. Emp. Ret. Fund*, 2018 WL 1384564 (2018) (Kagan, J.). The Court rejected the issuer’s argument that the Securities Litigation Uniform Standards Act (“SLUSA”) passed in 1998 eliminated the jurisdiction of state courts to hear such class actions. In resolving a split among state and federal courts, the Court likewise rejected a middle-of-the-road position advanced by the Solicitor General that such actions should be removable from state to federal court.

Background

The ‘33 Act allows persons who acquire a registered security to bring suit against an issuer, underwriter, and numerous others for materially false or misleading statements or omissions made in a registration statement or offering document. As originally passed, the ‘33 Act provided for concurrent jurisdiction, meaning that a plaintiff could bring such a claim in either state or federal court.

In 1995, Congress passed the Private Securities Litigation Reform Act (“PSLRA”) to combat the “nuisance filings, targeting of deep-pocket defendants, vexatious discovery requests, and ‘manipulation by class action lawyers of the clients whom they purportedly represent’” that had become a known feature of private securities litigation. *Merrill Lynch, Pierce, Fenner, & Smith v. Dabit*, 547 U.S. 71 (2006). The PSLRA instituted significant changes to class actions brought under federal securities statutes, including the ‘33 Act. Because these class action reforms generally applied only to cases brought in federal court, however, the PSLRA had an unintended consequence: plaintiffs bringing securities fraud class actions could avoid the PSLRA’s new restrictions by bringing their claims in state court, asserting claims under state law or under the ‘33 Act.

Concerned that the intent of the PSLRA was not being fully effectuated, Congress passed SLUSA in 1998. SLUSA’s “core provision” is § 77p, in which SLUSA divested state courts of the ability to hear class actions bringing state law claims involving “covered securities.” *Merrill Lynch*, 547 U.S. 71. Generally, a security is a “covered security” if it was listed on a national stock exchange at the time the alleged misrepresentation, omission, or deceptive conduct occurred.

§ 77p Does Not Limit State Court Jurisdiction Over Class Actions Alleging Only '33 Act Claims

The question before the Court was “whether § 77p limits state court jurisdiction over class actions brought under” the '33 Act.

The Court held that the provision of SLUSA in dispute does not deprive state courts of their concurrent jurisdiction over class actions alleging violations of the '33 Act. That provision provides that federal district courts “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” the '33 Act. 15 U.S.C. § 77v(a) (2012) (emphasis added). The Court termed the italicized language of this provision the “except clause,” and the central dispute in the case was whether the clause’s reference to “covered class actions” pointed to the definition of that term in § 77p(f)(2). If it did, Petitioners argued, state courts would not have jurisdiction over such class actions brought under the '33 Act.

The Court rejected Petitioners’ argument for two reasons. First, if Congress had wanted to refer to § 77p(f)(2)—instead of more broadly to § 77p, as it did in the except clause—it would have done so, “just by adding a letter, a number, and a few parentheticals.” Indeed, elsewhere in SLUSA Congress did use a pinpoint reference to a subsection of § 77p, the Court noted. Second, § 77p(f)(2) provides a *definition* (of “covered class action”) not an *exception* to concurrent jurisdiction, and Congress is well aware of the difference between those two functions.

The Court reasoned that, by its terms, § 77p only prevents certain class actions based on state law from being heard in state courts (the statute requires that they be removed to federal court and dismissed), and that nothing in the text prevents a state court from hearing class actions based exclusively on federal law.

Turning from the statutory language, the Court concluded that even if arguments about SLUSA’s legislative purpose and history could overcome a plain reading of the statutory text, Cyan failed to account for other ways in which SLUSA furthers Congress’s objectives. SLUSA’s preamble sets out the statute’s goal of “limit[ing] the conduct of securities class actions under State law.” In barring class actions brought under state law, SLUSA guarantees that the substantive protections of the federal Reform Act will apply to class actions, regardless of whether they proceed in state or federal court. This objective does not depend on stripping state courts of jurisdiction over '33 Act class actions.

Moreover, the Court wrote, SLUSA’s revisions to the Securities Exchange Act of 1934 (“the '34 Act”) served Congress’s goal of moving the majority of securities class actions to federal court. As with the '33 Act, SLUSA also amended the '34 Act to bar class actions based on state law, forcing plaintiffs to bring claims under the '34 Act. Because federal courts are vested with exclusive jurisdiction over '34 Act claims, those plaintiffs end up in federal, not state, court. And far more suits are brought under the '34 Act, which regulates all trading of securities, than the '33 Act, which regulates only securities offerings.

Finally, the Court rejected the Solicitor General’s “halfway-house position,” holding that SLUSA does not permit the removal of class actions alleging only '33 Act claims from state to federal court. Under that interpretation, another provision of § 77p in subsection (c) would permit the removal of '33 Act class actions to federal court if they allege false statements or deceptive devices in connection with the purchase of a covered security, as listed in § 77p(b). But § 77p(b) refers to *state-law* class actions, which are removable to federal court (after which they are to be dismissed), not *federal-law* class actions asserting '33 Act claims. The Court explained that the government’s construction distorted SLUSA’s text, and statutory language cannot be ignored “based on an intuition that Congress must have intended something broader.”

[1] Simpson Thacher filed a brief in this case on behalf of amici curiae in support of Petitioners.

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