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State Section 11 Litigation in the Post-*Cyan* Environment (Despite *Sciabacucchi*)†

By Michael Klausner, Jason Hegland,** Carin LeVine,*** and Jessica Shin*****

In Cyan, Inc. v. Beaver County Employees Retirement Fund, *the U.S. Supreme Court held that the Securities Litigation Uniform Standards Act of 1998 ("SLUSA") preserved state courts' jurisdiction to adjudicate cases brought under the Securities Act of 1933, with defendants having no right to remove a case to federal court. The result of this decision has been a dramatic increase in section 11 cases litigated in state court, often with a parallel case brought in federal court against the same defendants based on the same alleged misstatements. Just weeks ago, in* Salzberg v. Sciabacucchi, *the Delaware Supreme Court mitigated the impact of* Cyan *by upholding the facial validity of charter provisions requiring section 11 cases to be brought in federal court. That case provides some relief for Delaware corporations that have recently issued securities, or that plan to do so, if they have federal-forum charter provisions in place. The reach of* Sciabacucchi, *and the extent to which section 11 cases continue to be litigated in state court, will depend on a number of factors, most importantly the extent to which states in which these cases are litigated treat federal-form provisions as valid. Federal legislation, therefore, remains the most effective means of stemming the inefficiencies that this article documents empirically.*

Introduction

In *Cyan, Inc. v. Beaver County Employees Retirement Fund*, decided roughly two years ago, the U.S. Supreme Court held that plaintiffs may bring class actions in state court under the Securities Act of 1933 ("Securities Act").[1] Section 11 of the Securities Act provides a cause of action for misstatements and omissions in registration statements filed in connection with a public offering of securities,[2] and section 12(a)(2) provides a cause of action for misstatements and omissions in a prospectus or oral statements made in connection with a public offering.[3] The

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1. 138 S. Ct. 1061 (2018).
2. 15 U.S.C. § 77k (2018).
3. *Id.*

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vast majority of these cases allege violations of section 11.[4] Before *Cyan*, some state courts heard section 11 cases and some did not, depending on whether their state's federal district courts interpreted the Securities Litigation Uniform Standards Act ("SLUSA")[5] as requiring them to remand section 11 cases back to state court in response to a defendant's removal. In *Cyan*, the Court held that SLUSA did not withdraw jurisdiction over section 11 cases from state courts, and that federal courts must remand those cases back to state court. As a result, plaintiffs may now litigate section 11 class actions in state court, federal court, or both simultaneously for the same underlying violations. The *Cyan* decision has made section 11 litigation considerably more complicated and presumably more expensive for defendants; it has raised challenges for courts with respect to judicial efficiency; and it has enhanced opportunities for plaintiffs' lawyers to profit from filing cases of questionable merit.

On March 19, 2020, in *Salzberg v. Sciabacucchi*,[6] the Delaware Supreme Court upheld the facial validity of charter provisions that require Section 11 claims to be filed in federal court ("federal-forum provisions" or "FFPs"). The *Sciabacucchi* case will mitigate the impact of *Cyan*. So long as other state courts accept the validity of FFPs, they will dismiss section 11 cases filed against Delaware corporations with FFPs in their charters, and section 11 litigation against these companies will be limited to federal court. Companies going public, those planning mergers in which they will issue shares, and those planning to issue securities in any other context should certainly adopt an FFP. There is no downside, and the provision may well protect the firm from inefficient and potentially abusive litigation.

The *Sciabacucchi* case, however, does not spell the end of section 11 litigation in state courts. First, the Delaware Supreme Court only upheld the facial validity of FFPs, which means it found that FFPs are valid in some, but not necessarily, all situations. The Court thus left open the possibility that FFPs will be ruled invalid in particular contexts, in which case state litigation against a Delaware corporation could proceed notwithstanding an FFP, even in a case filed in Delaware state court. Second, there is no assurance that other states will accept the validity of FFPs in the charters of Delaware corporations, facially or as applied. If a state court concludes that a Delaware corporations' FFP is invalid, it will allow the case to proceed. We could therefore find ourselves in a situation similar to where we were prior to *Cyan*, where some states recognize FFPs as valid and some do not—and where plaintiffs' attorneys understandably try to file state cases in the latter. Third, at this point, FFPs have not been validated in states other than Delaware. Companies preparing to issue securities, therefore, will

4. *Id.* § 771(a)(2). Since 2011, there have been only three cases filed in state court alleging section 12(a)(2) violations without also alleging section 11 violations. For simplicity, we refer to all Securities Act cases as "section 11" cases throughout this article. However, the points we make and data we report will cover all cases alleging section 11 and/or section 12(a)(2) violations.

5. Pub. L. No. 105-353, 112 Stat. 3227 (1998) (codified as amended in scattered sections of 15 U.S.C.).

6. Salzberg v. Sciabacucchi, No. 346, 2019 (Del. Mar 18, 2020).

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presumably incorporate in Delaware and adopt FFPs. This could lead other state legislatures to validate FFPs, but at this point we do not know how this will play out. Accordingly, federal legislation that accomplishes what Congress intended to accomplish in SLUSA would be the most effective way to address the problems that we document when section 11 cases are litigated in state court.

In this article, we use the Stanford Securities Litigation Analytics ("SSLA") database to analyze section 11 cases in state courts before *Cyan* and in the two years since *Cyan*.[7] First, we look at the increase in the filing volume of section 11 cases in state courts since *Cyan*. Second, we look at the outcomes of state section 11 cases to determine how dismissal rates and settlement sizes in state courts compare with section 11 cases brought solely in federal courts. Third, we investigate how state and federal courts have managed section 11 litigation. Specifically, we look at pleading rules, the use of discovery stays, and the handling of parallel litigation where different plaintiffs' lawyers have filed cases in state and federal court based on the same alleged facts.

Part I of this article explains the state court procedural rules that raise concerns regarding section 11 litigation. Part II provides data on the explosion of section 11 litigation in state court following *Cyan*. Part III analyzes the outcomes of section 11 cases litigated in state court compared with those litigated in federal court. Part IV analyzes cases litigated in state and federal court simultaneously, with respect to both the outcomes of those cases and with respect to how state and federal courts have managed or declined to manage this parallel litigation. Our empirical analysis covers the period from January 1, 2011, through December 31, 2019.

I. Background: Concerns Regarding Procedural Rules in State Section 11 Litigation

Section 11 provides a monetary remedy to shareholders who purchase shares directly in a public offering or traceable to a public offering. Typically, a section 11 suit is brought as a class action, with the class consisting of those shareholders. Although the substance of section 11 is the same regardless of whether a case is litigated in state or federal court, more plaintiff-friendly procedural rules in state court can have a significant impact on litigation costs to defendants, on the value of a suit to plaintiffs and their attorneys, on judicial efficiency, and on the opportunity for plaintiffs and plaintiffs' lawyers to profit from filing weak cases. Those

7. *Stanford Securities Litigation Analytics*, Stan. L. Sch., https://sla.law.stanford.edu (last visited Jan. 9, 2020). The primary sources of data are federal and state court dockets. In some instances, state court documents are not electronically available, in which case we rely on company disclosures and other information sources to fill in missing information.

The analysis in this article covers securities class actions filed in federal and state court against publicly traded companies between January 1, 2011, and December 31, 2019, that allege misstatements or omissions related to public offerings of securities in violation of either section 11 or 12 of the Securities Act of 1933. We exclude (i) actions related to initial coin offerings (ICOs), which raise new issues unrelated to the advent of state section 11 litigation that would confound comparisons between state and federal cases; (ii) cases involving solely unregistered securities; and (iii) cases that name only third-party defendants, such as underwriters and auditors.

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procedural rules are: pleading standards governing motions to dismiss; the timing of discovery in relation to rulings on the motion to dismiss; and the coordination (or not) of parallel state and federal cases.

A. Pleading Standards

As applied to section 11 cases, state court pleading standards will be an important factor in determining the impact of litigating section 11 cases in state courts nationwide. Federal courts follow the *Twombly–Iqbal* pleading standard, under which a plaintiff can withstand a motion to dismiss only by alleging "enough facts to state a claim to relief that is plausible on its face"[8] in light of "judicial experience and common sense."[9] Facial plausibility is satisfied when a complaint permits a "court to draw the reasonable inference that the defendant is liable for the misconduct alleged."[10] Conclusory statements are insufficient to demonstrate facial plausibility.[11] Federal courts applying this pleading standard to cases raising solely section 11 claims have granted motions to dismiss in 38 percent of rulings since 2011.

In contrast, many states generally follow a more lenient pleading standard than the *Twombly–Iqbal* plausibility standard.[12] In California—where section 11 cases had been litigated for several years before *Cyan*—a plaintiff must merely plead a "statement of the facts constituting the cause of action, in ordinary and concise language."[13] In New York, where 40 percent of section 11 cases have been filed since *Cyan*, the pleading standard is more stringent than the California standard but still more lenient that the federal standard.[14] In Part III, we discuss

8. Bell Atl. Corp. v. Twombly, 550 U.S. 544, 570 (2007).

9. Ashcroft v. Iqbal, 556 U.S. 662, 679 (2009).

10. *Id.* at 678.

11. *Twombly*, 550 U.S. at 555; *Iqbal*, 556 U.S. at 678. In most federal circuits, section 11 cases that "sound in fraud" apply the higher pleading standard enacted in the Private Securities Litigation Reform Act of 1995, Pub. L. No. 104-67, 109 Stat. 737 (codified as amended in scattered sections of 15 U.S.C.) ("PSLRA"). That pleading standard requires that a complaint "state with particularity facts giving rise to a strong inference that the defendant acted with the required state of mind." 15 U.S.C. § 78u-4(b)(2)(A) (2018); *see, e.g.*, *In re* Fuwei Films Sec. Litig., 634 F. Supp. 2d 419, 436 (S.D.N.Y. 2009). Only the Eighth Circuit has consistently declined to apply this heightened standard. Amy L. Craiger, *From Conceivable to Impossible: The Hurdles Plaintiffs Must Overcome When Pleading Section 11 and Section 12(a) Securities Claims*, 5 Brook. J. Corp. Fin. & Com. L. 549, 556, 571 (2011). The *Tellabs* case added a gloss to the PSLRA's heightened pleading standard, requiring that the strong inference "must be more than merely plausible or reasonable—it must be cogent and at least as compelling as any opposing inference of nonfraudulent intent." Tellabs, Inc. v. Makor Issues & Rights, Ltd., 551 U.S. 308, 314 (2007). To avoid the higher pleading standard, however, plaintiffs' attorneys generally try not to plead fraud in section 11 cases.

12. *See* Jane Willis & F. Turner Buford, *Pleading Standards in the Federal and State Trial Courts: The Evolving Impact of U.S. Supreme Court Precedent*, Litig. Comment. & Rev. (Aug. 2009), https://litigationcommentary.org/2009/2009-august/109-pleading-standards-in-the-federal-and-state-trial-courts-the-evolving-impact-of-us-supreme-court-precedent. On the other hand, Massachusetts has explicitly adopted the *Twombly–Iqbal* standard. Iannacchino v. Ford Motor Co., 888 N.E.2d 879, 890 (Mass. 2008).

13. Cal. Civ. Proc. Code § 425.10 (Deering 2019).

14. N.Y. C.P.L.R. 3013 (Consol. 2019) (requiring a pleading to be "suffiently particular to give . . . notice of the . . . transactions or occurrences . . . and the material elements of each cause of action");

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how the California and New York courts and others have addressed motions to dismiss in section 11 cases since *Cyan*.

B. Discovery Stay

In federal court, there is an automatic stay of discovery under the PSLRA until a motion to dismiss is denied.[15] In combination with the *Twombly–Iqbal* pleading standard, the discovery stay poses a considerable hurdle for plaintiffs' attorneys, who must obtain detailed information about a defendant before discovery. With a 38 percent dismissal rate in federal court, this rule accounts for substantial savings in litigation expense for defendants, though plaintiffs' attorneys argue that it screens out meritorious cases. In contrast, state courts generally allow discovery to begin before they rule on a motion to dismiss.[16] All other factors being equal, an early start to discovery imposes costs on a defendant and creates pressure to settle a case before a ruling on a motion to dismiss.

The timing of discovery in section 11 cases litigated in state court will have a significant impact on section 11 litigation in state courts.[17] In Part III, we examine the extent to which state courts have adopted the PSLRA's discovery stay.

C. Coordination of Parallel State and Federal Cases

A third important procedural rule in securities class actions litigated in federal court is the process by which multiple cases are consolidated into a single case with lead plaintiffs and lead counsel selected.[18] Federal courts manage that process according to rules prescribed by the PSLRA.[19] States have their own consolidation processes when multiple class actions are brought within a single state, but where cases based on the same alleged violation are filed in multiple states

King v. Commercial Ins. Co., 275 N.Y.S.2d 975, 977 (App. Div. 1966); *see also* Lisa A. Zakolski & Judith Nichter Morris, Carmody Wait 2d New York Practice with Forms § 27:29 (2019).

15. 15 U.S.C. § 77z-1(b) (2018).

16. *See, e.g.*, Beaver Cty. Emps. Ret. Fund v. VHCP Mgmt., LLC, No. CIV536488 (Cal. Super. Ct. filed Dec. 7, 2015) (involving issuer defendant Avalanche Biotechnologies, Inc.); Geller v. Morris, No. CIV537300 (Cal. Super. Ct. filed Feb. 26, 2016) (involving issuer defendant LendingClub Corporation). On the other hand, some state courts have granted motions to stay discovery pending ruling on a motion to dismiss. *See* Order re Motion to Dismiss or Stay at 2, Book v. Pronai Therapeutics, Inc., No. 16CIV02473 (Cal. Super. Ct. Mar. 14, 2018) (No. 1031262); Endorsement on Motion to Stay Discovery, Carlson v. Ovascience Inc., No. 1584CV03087 (Mass. Super. Ct. June 2, 2016).

17. *See* Doug Greene, Jessie Gabriel, Marco Molina & Brian Song, *The Coming Securities Class Action Storm: Multijurisdictional Litigation After* Cyan, PLUS J., 3Q 2018, at 1, https://www.wileyrein.com/media/publication/486_Q32018.pdf; David M.J. Rein & Matthew A. Schwartz, *Expert Q&A on Securities Act Claims and SLUSA After* Cyan, Thomson Reuters Prac. L.J., June/July 2018, at 16, https://www.sullcrom.com/files/upload/Practical_Law_Rein_Schwartz_May2018.pdf.

18. 15 U.S.C. § 77z-1(a)(3)(B)(i)–(ii) (2018); Fed. R. Civ. P. 42(a); David M.J. Rein, Matthew A. Schwartz, & John P. Collins, Jr., *Securities Litigation Involving the Private Securities Litigation Reform Act (PSLRA)*, Thomson Reuters Prac. L.J., Oct./Nov. 2017, at 39, https://www.sullcrom.com/files/upload/ThomsonReutersJournal_Litigation_PSLRA_OctNov17.pdf. It is not unusual for a lead counsel to file a case with two or three lead plaintiffs.

19. The court accords a presumption in favor of selecting the plaintiff(s) with the "largest financial interest" in the case. 15 U.S.C. § 77z-1(a)(3)(B)(i), (iii)(bb) (2018); *see also* Rein & Schwartz, *supra* note 17; Rein et al., *supra* note 18.

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or in state and federal courts, the litigation can get complicated—and inefficient. Where plaintiffs file multiple cases in state courts of different states, the doctrine of *forum non conveniens* may relieve a defendant of the burden of litigating in multiple states, but there is no assurance that a court will provide that relief. Similarly, where cases are filed in state and federal courts, the state court may stay its proceedings pending resolution of the federal case. A federal court could also stay state court proceedings under section 27(b)(4) of SLUSA, which authorizes a federal court to stay state court discovery "in aid of its jurisdiction" if necessary.[20] Stays of these sorts are not the same as the federal court consolidation process, but their use would at least reduce the burden on defendants and the inefficiency of litigating the same case simultaneously in state and federal courts.

The extent to which state and federal courts use their powers to coordinate state and federal cases will have a substantial impact on the burden imposed on defendants and on the efficiency of section 11 litigation in the post-*Cyan* environment. In Part IV, we examine how courts have managed parallel state and federal litigation so far.

In the wake of *Cyan*, and notwithstanding *Sciabacucchi* these three procedural concerns raise serious issues regarding whether (a) state courts will filter out non-meritorious section 11 cases at the motion-to-dismiss stage, (b) defendants will incur discovery costs in cases that are ultimately dismissed, (c) defendants will face high litigation costs simultaneously defending cases in state and federal courts, and (d) cases of doubtful merit will be filed in state court in anticipation of plaintiff-friendly procedural rules.[21] In the remainder of this article, we investigate actual experience with state section 11 litigation to evaluate the extent to which it supports these concerns.

II. State Section 11 Filing Volume Since *Cyan*

For the reasons explained above, the volume of section 11 cases filed in state court was expected to increase as a result of *Cyan*. As Figure 1 shows, that expectation has been borne out. Figure 1 includes cases (i) filed solely in state court, (ii) filed solely in federal court, and (iii) filed in both state and federal court based on the same alleged misstatement or omission. Parallel cases in state and federal courts appear in Figure 1 as both state and federal cases.[22] There have been seventy-five cases filed in state court since *Cyan* was decided in early 2018—a sharp increase over prior years.[23] Among those cases, thirty

20. 15 U.S.C. § 77z-1(b)(4) (2018) ("Upon a proper showing, a court may stay discovery proceedings in any private action in a State court as necessary in aid of its jurisdiction, or to protect or effectuate its judgments, in an action subject to a stay of discovery pursuant to this subsection.").

21. Greene et al., *supra* note 17; Rein & Schwartz, *supra* note 17; *The Supreme Court's* Cyan *Decision and What Happens Next*, DavisPolk (Apr. 13, 2018), https://www.davispolk.com/files/2018-04-13-supreme-courts-cyan-decision-what-happens-next.pdf.

22. Cases filed in state court and successfully removed to federal court are counted as federal cases. Cases filed in multiple state courts based on the same allegations are counted as a single case in the year the first case was filed.

23. All but two of the state cases filed in 2018 were filed after the *Cyan* decision came out.

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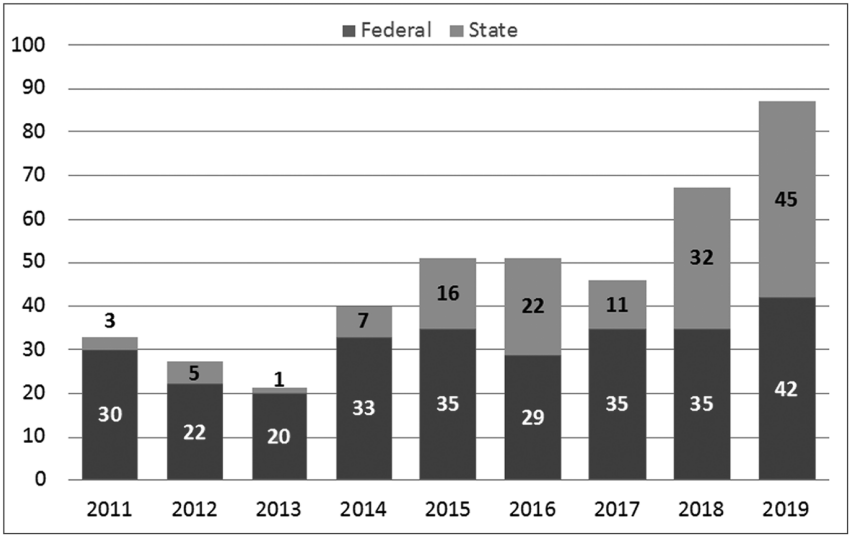
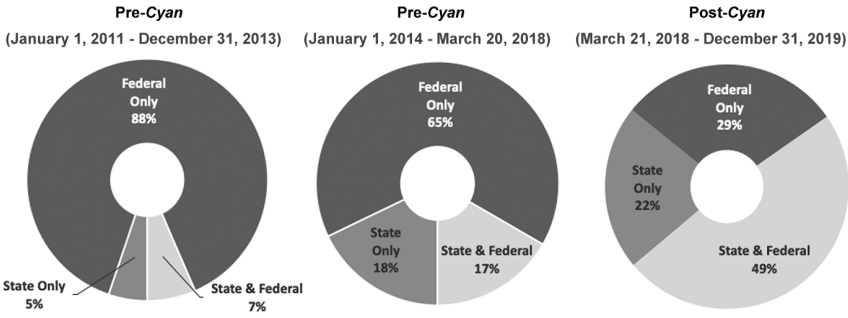
Figure 1
Forum Choice in Securities Act Cases Filed 2011 Through 2019



have been filed in New York, where defendants had successfully removed section 11 cases to federal court before *Cyan*, and twenty-five have been filed in California, which had previously heard the bulk of section 11 cases.

In Figure 2, which combines the pre-*Cyan* years into two periods for comparison with the post-*Cyan* period, we separate cases into those filed solely in state

Figure 2
Forum Mix in Securities Act Cases Filed 2011 Through 2019



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court, those filed solely in federal court, and parallel pairs of cases filed in both state and federal courts (where a parallel pair is reflected as one case in this chart). Since *Cyan*, cases filed exclusively in federal court comprise only 29 percent of section 11 filings, compared to 88 percent between 2011 and 2013 and 65 percent between 2014 and March 20, 2018, when *Cyan* was decided. Furthermore, the opening of state courts to section 11 cases has contributed to an increase in the total volume of section 11 litigation. This increase is not explained by an increase in public offerings. This suggests that the increases may have been driven by an increase in low-merit cases that are attracted to state courts by lenient procedural rules. We analyze evidence of this below.

III. Outcomes of State Section 11 Cases Filed Solely in State Court

In the analysis below, we focus on dismissal and settlement rates and on settlement size in state section 11 cases filed solely in state court since 2011. We compare those outcomes to outcomes in section 11 cases litigated solely in federal court. For purposes of these comparisons, we consider federal cases with section 11 claims only—that is, we omit from the analysis federal cases with both section 11 claims and claims under section 10(b) of the Securities Exchange Act of 1934.[24] While this allows for a rough apples-to-apples comparison between state and federal cases,[25] it also means we omit many federal cases with section 11 claims. Between 2011 and 2019, there were fifty-three federal cases with solely a section 11 claim and no parallel suit filed in state court, forty-eight of which have been resolved. There were 139 federal cases with both section 10(b) and section 11 claims filed during the same period, with no parallel state cases. Of those 139 cases, 104 have been resolved.[26]

Our comparison of outcomes in cases filed solely in state court with those filed solely in federal court is confounded by two cross-cutting potential effects. On one hand, we are comparing the impact of plaintiff-friendly procedural rules in state court with stricter rules in federal court. We expect those differences to result in better state-court outcomes for plaintiffs. On the other hand, we expect that, on the whole, cases filed solely in state court may be weaker than cases filed solely in federal court. Not only would relatively weak procedural rules attract weak cases, but for a case to be filed *solely* in state court, it must be true that no plaintiffs' lawyer deemed it worthwhile to file a parallel case in federal court. The strength of a case presumably influences its outcome. Consequently, the differences in outcomes will reflect the net impact of the procedural differences and the selection effect that those procedural differences produce. In

24. 15 U.S.C. § 78j(b) (2018).

25. As we explain below, there may be selection effects with respect to plaintiffs' attorneys filing cases in either state or federal court, which would mean we do not have a perfect apples-to-apples comparison of state and federal court treatment of section 11 cases.

26. In this section, events in a case are reported as of December 31, 2019.

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addition, because a large majority of cases filed in state court are California cases, our results are heavily influenced by what has occurred in California state courts.

A. Dismissal and Settlement Rates

As explained above, the differences in generally applicable pleading standards between state and federal courts mean that unless states adopt higher pleading standards for section 11 cases, dismissal rates will be lower in state court than in federal court, all other factors held constant. Holding all factors constant, however, may not be possible due to the selection effect that may drive cases into state court. We nevertheless compare final rulings on motions to dismiss and present those results in Table 1.[27] Notwithstanding the possibility that state cases may be weaker than federal cases, the dismissal rate in state court has been lower than in federal court—28 percent of motions to dismiss have been granted in state court, compared to 39 percent in federal court. If we include federal cases with section 10 and section 11 claims, the dismissal rate for those cases remains at 39 percent.[28] The low dismissal rate in state court is driven by California cases, which constitute a large majority of resolved state court cases. In cases filed solely in state court since 2011, California courts have granted motions to dismiss in only 18 percent of cases—and only 12 percent of cases if one includes those with parallel federal cases.

Table 2 shows all possible outcomes: settlements, dismissals, and dropped cases. This analysis is complicated by the fact that in some pending cases—both

Table 1

Rulings on Motions to Dismiss in Cases Filed 2011 Through 2019

		MTD Granted	MTD Denied	Total
State	n	8	21	29
	%	*(28%)*	*(72%)*	*(100%)*
Federal	n	13	20	33
	%	*(39%)*	*(61%)*	*(100%)*

27. This table includes only cases in which there has been a ruling on a motion to dismiss. We treat motions to dismiss as granted if either (a) the motion was granted with prejudice or (b) the motion was granted without prejudice and the plaintiff did not refile a complaint. If a motion was granted without prejudice and the plaintiff refiled a complaint but later dropped the case, that outcome is not treated as a motion to dismiss having been granted but rather as a dropped case and is excluded from the total in Table 1. Dropped cases are picked up in Table 2, as are cases that settled before a final ruling on a motion to dismiss.

28. In the small sample included in Table 1, where federal cases have only section 11 claims, the difference between state and federal dismissal rates is not statistically significant—the *p-value* is .138. If we include cases filed in both state and federal courts, the lower dismissal rate in state court is statistically significant at the 5 percent level.

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Table 2

Outcomes in Cases Filed and Resolved from 2011 Through 2019[29]

		Dismissed	Settled*	Dropped	Total
State	n	8	24	4	36
	%	(22%)	(67%)	(11%)	(100%)
Federal	n	13	31	4	48
	%	(27%)	(65%)	(8%)	(100%)

* This count of settled actions includes pending cases—four state cases and one federal case—that have survived a motion to dismiss and continued to discovery. In the SSLA database of cases filed January 2000 to the present, there are only two cases with solely section 11 claims in which defendants ultimately prevailed following the denial of a dismissal motion.

state and federal—motions to dismiss have already been denied with prejudice and therefore the case will settle at some point. We therefore include those cases in the "Settled" column.[30] Although the rate at which motions to dismiss are granted in state court is substantially lower than in federal court, the percentage of cases that settle is essentially the same—67 percent in state court and 65 percent in federal court. This is because many federal cases settle before reaching a ruling on a motion to dismiss. Our data show that 35 percent of federal court settlements occur before a final ruling on a motion to dismiss, while only 20 percent of state court settlements do. The fact that the settlement rate in federal court is the same as that in state court despite the relatively strict procedural hurdles suggests that cases brought in federal court may be stronger than those brought in state court. The more plaintiff-friendly rules in state court may thus be attracting cases of relatively low merit. We continue to investigate that possibility in Section B, below, where we compare settlement sizes.

Might state pleading standards and discovery rules change as state courts continue hearing section 11 cases nationwide? Perhaps. There are some positive signs. One positive sign with respect to pleading standards is a post-*Cyan* New York case, *In re Dentsply Sirona, Inc. Shareholders Litigation*.[31] In *Dentsply Sirona*, Judge Scarpulla dismissed a complaint alleging that the defendants' registration statement had failed to disclose information required by Items 303 and 503 of Securities and Exchange Commission ("SEC") Regulation S-X.[32] Those provisions require a company to disclose, respectively, "known trends having an impact on sales, revenues or income" and "the most significant factors that make the offering

29. In Table 2, we show thirteen federal cases dismissed, whereas in Table 1, we show fourteen motions to dismiss granted. The discrepancy is due to the fact that there is one case in which the motion to dismiss was granted and the parties settled while the dismissal was on appeal. We therefore treat that case as settled.

30. Pending cases in which there has been no final ruling on a motion to dismiss are omitted from the figure.

31. No. 155393/2018 (N.Y. Sup. Ct. filed June 7, 2018).

32. *See* 17 C.F.R. §§ 229.303, 229.503 (2020).

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speculative or risky."[33] With respect to "known trends,"[34] the court held that the plaintiffs had failed to "plead, with some specificity, facts establishing that defendant had actual knowledge of the purported trend."[35] The court held as well that the plaintiffs had failed to allege with sufficient specificity the defendants' failure to disclose relevant risk factors.[36] Forty percent of post-*Cyan* state cases have been filed in New York, which had heard no section 11 cases before *Cyan*. So this case could well pave the way for similar rulings in New York and may influence other state courts.

Even in California, which has applied its ordinary, permissive pleading standard to section 11 cases since it started hearing these cases well before *Cyan*—and has denied motions to dismiss in 88 percent of its cases—one court has taken a different approach in a post-*Cyan* case. In *In re Natera Securities Litigation*. Judge Buchwald dismissed a complaint that also alleged a misstatement with respect to Item 303 of Regulation S-X.[37] In so doing, he exercised judicial notice in reviewing the defendant's motion to a degree not ordinarily exercised by California courts. Judge Buchwald stated:

> [T]he Court believes that it has the discretion, under California's complex case [] rules to treat the pending Motion as would a Federal trial court when hearing and deciding a Rule 12(b) Motion to Dismiss . . . .
>
> . . . .
>
> Using this Federal motion procedure is also now even more warranted in the wake of the recent United States Supreme Court decision in *Cyan, Inc. v. Beaver County Employees Retirement Fund* (2018) 138 S. Ct. 1061 validating the concurrent Federal and State court jurisdiction over 1933 Act cases . . . . This recent confirmation of concurrent jurisdiction would appear to call for some consistency and uniformity in the handling of such cases as between the Federal and State Courts.
>
> . . . .
>
> [T]he *Cyan* decision clearly contemplates uniform treatment of securities class actions in Federal and State courts, [so] it makes sense to apply here . . . the broader scope of judicial notice routinely used on early pleading motions in Federal courts.[38]

Applying this approach to judicial notice rather than the more restrictive approach that California courts generally apply, Judge Buchwald held that the plaintiffs' allegation of knowledge was "at direct odds with judicially noticeable evidence"[39] and dismissed the complaint.

In addition, post-*Cyan* cases provide some hope for state courts granting stays of discovery pending rulings on motions to dismiss. Since *Cyan*, there

33. *Id.* § 229.503(c).
34. *Id.* § 229.303(4)(i)(D).
35. *See* Decision and Order on Motion at 13, *In re* Dentsply Sirona, Inc. S'holders Litig., No. 155393/2018 (N.Y. Sup. Ct. Sept. 26, 2019) (No. 180) (quoting Opinion and Order at 7, *In re* Jumei Int'l Holdings Sec. Litig., No. 14-CV-09826 (S.D.N.Y. Jan. 10, 2017) (No. 105)).
36. *Id.* at 14.
37. No. CIV537409 (Cal. Super. Ct. filed Mar. 24, 2016).
38. Memorandum of Decision and Order at 4–5, *In re* Natera Sec. Litig., No. CIV537409 (Cal. Super. Ct. Aug. 7, 2018) (No. 1309959).
39. *Id.* at 9.

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have been fifteen rulings in state courts on motions to stay discovery, ten of which were in New York. Of the ten New York rulings, four were granted, four were denied, and two were granted pursuant to the parties' stipulations. In one of the New York cases, and in a Connecticut case, the courts held that the language of the PSLRA's mandatory stay provision—which begins, "In *any* private action arising under this subchapter . . ."[40]—applies to cases tried in state courts.[41] In *In re Everquote*, New York Judge Borrock stated: "The simple, plain, and unambiguous language [of the PSLRA] expressly provides that discovery is stayed during a pending motion to dismiss '[i]n any private action arising under this subchapter.'"[42] Similarly, in the *Pitney Bowes* case, Connecticut Judge Lee held that the language of the PSLRA "compels the conclusion" that the discovery stay applies in state court.[43] In another New York case, *In re Greensky*, Judge Schecter stated that she was "not convinced that the PSLRA, by its terms, expressly mandates a stay in state court" but that "[t]he important purpose underlying enactment of the automatic stay—ensuring that cases have merit at the outset—should not be disregarded merely because a federal cause of action is being prosecuted in state court."[44] On the other hand, New York Judge Scarpulla has twice rejected the argument that the PSLRA discovery stay applies in state cases, simply asserting that "[a]pplication of the federal PSLRA's discovery stay would undermine *Cyan's* holding that '33 Act cases can proceed in state courts."[45] Other state courts have also denied motions to stay discovery.[46]

B. Settlement Size

In this section, we compare settlement size in state and federal cases, again looking at cases filed solely in state or federal court—and again, where a large majority of resolved state cases are in California. The implications of plaintiff-friendly state pleading standards and discovery rules for the size of settlements

40. 15 U.S.C. § 77z-1(b)(1) (2018) (emphasis added).

41. *See* Decision and Order at 11, *In re* Everquote, Inc. Sec. Litig., No. 651177/2019 (N.Y. Sup. Ct. Aug. 6, 2019) (No. 73).

42. *Id.*

43. *See* Memorandum of Decision Re Defendants' Motions for Protective Order Staying Discovery Pursuant to 15 U.S.C. Section 77z-1(b)(1) (#135 and #143) at 7–8, City of Livonia Retiree Health & Disability Benefits Plan v. Pitney Bowes Inc., No. FST-CV-18-6038160-S (Conn. Super. Ct. May 15, 2019) (No. 135.01).

44. *See* Decision and Order at 3, *In re* Greensky, Inc. Sec. Litig., No. 655626/2018 (N.Y. Sup. Ct. Nov. 25, 2019) (No. 91).

45. *See* Decision and Order on Motion at 14, *In re* Dentsply Sirona, Inc. S'holders Litig., No. 155393/2018 (N.Y. Sup. Ct. Aug. 2, 2019) (No. 174); Decision and Order at 12–13, *In re* PPDAI Grp. Sec. Litig., No. 654482/2018 (N.Y. Sup. Ct. July 5, 2019) (No. 91).

46. *See, e.g.,* Order Denying Defendants Arcimoto, Inc., Mark Frohnmayer, Douglas M. Campoli, Thomas Thurston, Terry Becker and Jefferson Curl's Motion to Stay Further Discovery Pending Ruling on Demurrer, Switzer v. W.R. Hambrecht & Co., No. CGC18564904 (Cal. Super. Ct. Sept. 19, 2018) (No. 001C06502186) (involving issuer defendant Arcimoto, Inc.); Order Denying Motion to Stay Proceedings at 2–3, Buelow v. Alibaba Grp. Holdings Ltd., No. CIV535692 (Cal. Super. Ct. Apr. 1, 2016); Order Denying Defendant's Motion to Stay Proceedings at 3–4, Young v. Pac. Biosciences of Cal., Inc., No. CIV509210 (Cal. Super. Ct. May 24, 2012).

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we observe are once again ambiguous. On one hand, a lower likelihood of dismissal in state court—especially when coupled with early discovery—would give plaintiffs greater leverage to extract a settlement than they would have in federal court. But this leverage would only last until a ruling on a motion to dismiss. After the ruling, state and federal cases would be on equal footing from the perspective of the procedural rules discussed in Part I. On the other hand, for the reasons explained above, cases filed solely in state court may be relatively weak, in which case we could well observe *lower* settlements in state court than in federal court—especially for cases that settle after a ruling on a motion to dismiss. Presumably, the merits do matter in negotiating a settlement.

Table 3 compares settlement size in state and federal cases—both in dollar amounts and as a percentage of statutory damages, which we estimate as the difference between the price of a defendant's shares in its public offering and the market value of those shares at the time of a lawsuit. Consistent with our analysis of dismissal rates, and to maintain an apples-to-apples comparison, we include among federal cases only those with solely a section 11 claim. Both in dollar value and as a percentage of statutory damages, the median settlements are essentially the same in state and federal court. But the mean settlement in state court is much lower than the mean in federal court. The difference in means reflects the fact that federal cases include more large settlements than do state cases. This difference in state and federal court settlement size is consistent with the selection effect discussed above—relatively weak cases being brought in state court.

To look more closely at whether there is a selection effect driving weaker cases into state court, we look at settlements that occur after motions to dismiss have been denied—when the state procedural rules discussed above would not create pressure on defendants to settle. The results of this comparison are presented in Table 4. Among those cases, the mean dollar amount of settlements in federal cases is more than twice the mean of state cases, but the medians are essentially the same—again reflecting a substantially skewed distribution of federal

Table 3

Settlements in Cases Filed and Resolved from 2011 Through 2019

	Total Settlement in Dollars	
	State	Federal
Mean	$7,941,875	$17,900,000
Median	$7,800,000	$7,500,000
	Recovery as a Percent of Statutory Damages	
Mean	12.4%	27.5%
Median	11.0%	11.0%
Observations	20	31

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Table 4

Settlement Size in Cases Settled After Motion to Dismiss Ruling—Cases Filed 2011 Through 2019

	Total Settlement in Dollars	
	State	Federal
Mean	$8,317,969	$21,100,000
Median	$8,275,000	$7,750,000
	Recovery as a Percent of Statutory Damages	
Mean	12.6%	37.3%
Median	11.0%	20.0%
Observations	16	20

settlements toward the high end when measured in dollar amounts. But when settlements are measured as a percentage of potential statutory damages, both the mean and median settlements in state cases are much lower than those in federal cases. These findings further suggest that state courts have attracted weaker cases than those filed in federal court.

In sum, the outcomes of cases filed solely in state court—most of which are in California state court—are consistent with concerns regarding the leniency of state procedural rules toward plaintiffs. State courts have dismissed cases far less frequently than do federal courts. Furthermore, the leniency of state court rules appears to have attracted cases to state court that are weaker than those brought in federal court.

IV. Litigation of Parallel Pairs of State and Federal Cases

In the discussion below, we address the most complex aspect of the post-*Cyan* legal environment: litigating parallel lawsuits in state and federal courts. We define a federal case as parallel to a state section 11 case if the two cases include a cause of action based on the same alleged misstatements or omissions in the defendant's registration statement.[47] When parallel cases are filed in state and federal courts, the lead counsel and lead plaintiff are different, and counsel for the parallel cases generally do not coordinate with one another. Whereas the analysis in Part III required that we exclude federal cases with section 10(b) claims, the analysis below will include pairs of cases where the federal case has any of the following: (i) only a section 11 claim, (ii) only section 10(b) claims, or (iii) both section 11 and section 10(b) claims. Where the federal case includes section 10(b) claims, there typically is one claim based on offering documents

47. With respect to the three cases with section 12 counts and no section 11 counts, we define a parallel federal case as one that includes the same alleged misstatements or omissions in the prospectus or oral statement.

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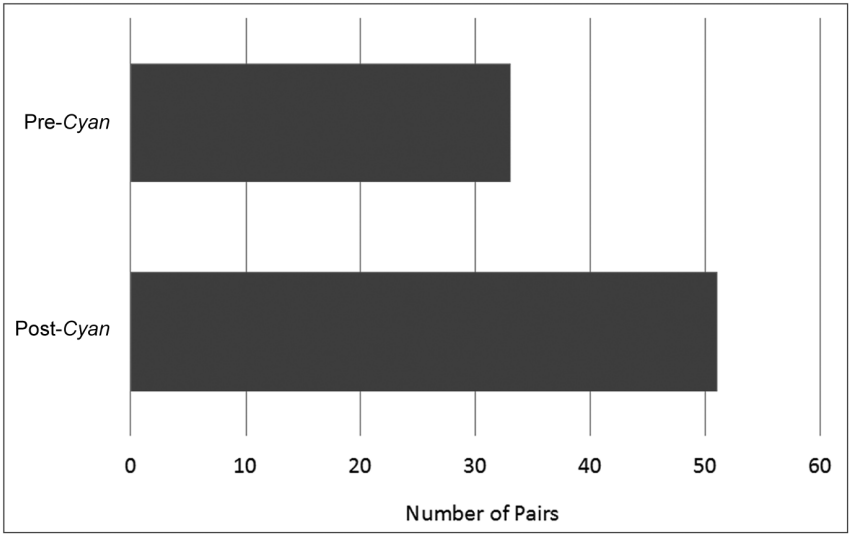
and additional claims based on alleged misstatements or omissions that occurred after the company went public. Throughout Part IV, we will refer to parallel lawsuits filed in state and federal court as "parallel pairs" or "pairs" of cases.

Since 2011, eighty-four parallel pairs have been filed. As shown in Figure 3, fifty-one of those have been filed since March 20, 2018, when *Cyan* was decided.[48] Twenty-eight of the eighty-four have been resolved—meaning that both the state and federal cases have been resolved. Thirteen of those are post-*Cyan* resolutions.

Figure 4 shows the outcomes of the twenty-eight parallel pairs that have been resolved as of the end of 2019. We treat a parallel pair as "dismissed" if a motion to dismiss has been granted in either the state or the federal case and the other case is either dismissed or voluntarily dropped. Recall from Table 2 that 67 percent of cases filed solely in state court and 65 percent of cases filed solely in federal court settled. In contrast, 82 percent of parallel pairs (23 out of 28) settled. This high rate of settlement is due in large part to California courts' disinclination to dismiss cases, as discussed in Part III, but the difference in settlement

Figure 3
Parallel Pairs Filed 2011 Through 2019



48. This figure includes six pairs where one case was filed before *Cyan* was decided and the other after. In the remaining forty-five pairs, both federal and state cases were filed before *Cyan*. It also includes two pairs in which one of the paired cases was outside our sample range of 2011 through 2019.

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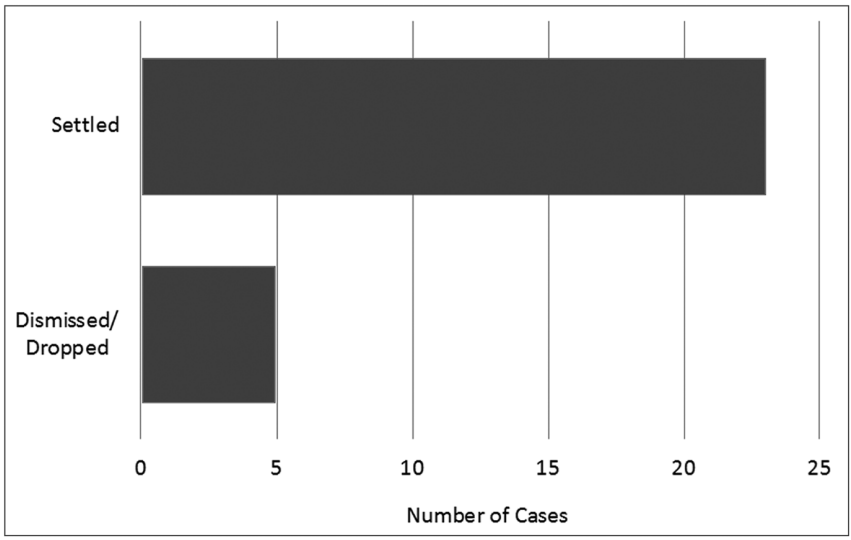
Figure 4
Outcomes of Parallel Pairs Filed 2011 Through 2019



rates between cases litigated solely in state court and those litigated in parallel pairs presumably reflects as well the costs defendants face litigating simultaneously in state and federal court.

In litigating parallel cases in state and federal courts, there are tools potentially available to a defendant that can reduce litigation costs and the resultant pressure to settle—and enhance judicial efficiency as well. The tool that has been most successful—though by no means universally successful—has been a motion in state court to stay that court's proceedings pending resolution of the parallel federal case, or pending the federal court's ruling on its motion to dismiss.[49] These stays do not necessarily end the state case; if a state court grants a stay, the case can still be revived at a later time. Even if the federal case is dismissed, the state court may then lift its stay and proceed to rule on its own motion to dismiss. Because the federal plaintiff class will not be certified before the federal court's dismissal, the federal court's ruling will not have a preclusive effect on the

49. One California state court has occasionally stayed its proceedings on grounds of *forum non conveniens* when the parallel federal case is in another state. In those cases, the court has allowed the parties to return to court at any time to petition to have the stay lifted. So long as the stay remains in place and the plaintiffs do not refile a case in another state, these stays have the same effect as a stay pending resolution of the parallel federal case. *See* Order Granting Motion to Stay for *Forum Non Conveniens* at 1–2, Cervantes v. Allen & Co., No. Civ. 534768 (Cal. Super. Ct. Feb. 29, 2016) (involving issuer defendant Etsy, Inc.); Case Management Order #6 at 8–11, Ragsdale v. Micro Focus Int'l PLC, No. 18CIV01549 (Cal. Super. Ct. Dec. 3, 2018) (No. 1524575).

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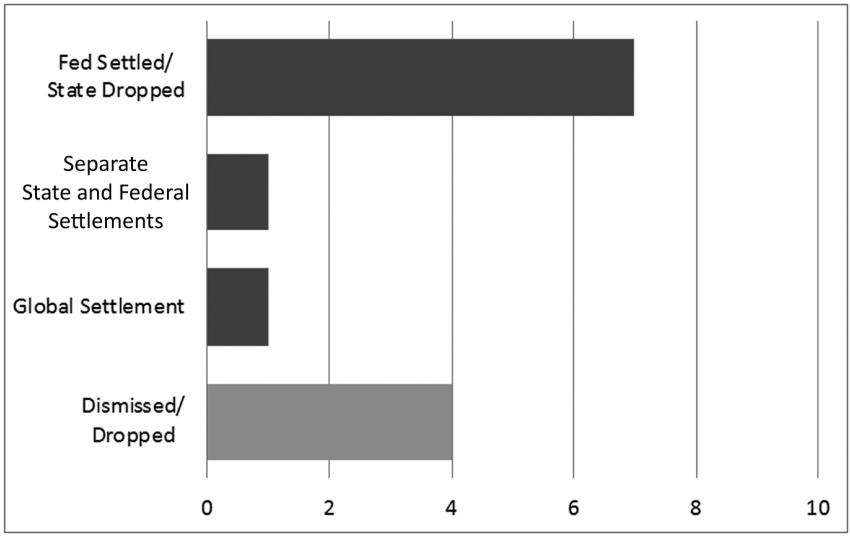
state case. Nonetheless, the state court may be influenced by the federal dismissal, and the defendant at least has the opportunity to negotiate a settlement before state discovery costs mount.

There have been twenty-seven cases in which courts have granted motions to stay a state case pending resolution of a parallel federal case or pending a ruling on a motion to dismiss the federal case,[50] and there have been twenty-six cases in which those motions were denied.[51] Of the twenty-seven pairs in which stays have been granted, thirteen have been resolved. Figure 5 shows the outcomes of those thirteen parallel pairs. These resolutions demonstrate how a stay can promote relatively efficient resolution of parallel litigation. As Figure 5 shows,

Figure 5
Outcomes of Parallel Pairs Where the State Case Was Stayed



50. *See, e.g.*, Decision and Order on Motion at 12–13, Mahar v. Gen. Elec. Co., No. 653648/2018 (N.Y. Sup. Ct. Oct. 15, 2019) (No. 155) (stay pending resolution of federal case); Order Re: Motions to Stay at 4–5, *In re* Arlo Techs., Inc. S'holder Litig., No. 18cv339231 (Cal. Super. Ct. June 21, 2019) (No. 3037496) (same); Order Granting Motion for a Stay of Proceedings at 1, Reyes v. Zynga Inc., No. CGC12522876 (Cal. Super. Ct. Aug. 26, 2013) (No. 001C04178178) (stay pending federal court ruling on motion to dismiss); Order, Rajasekaran v. Cytrx Corp., No. BC541426 (Cal. Super. Ct. Oct. 14, 2014) (same).

51. *See, e.g.*, Order After Hearing on October 25, 2019 at 6–8, Franchi v. Cloudera, Inc., No. 19CV348674 (Cal. Super. Ct. Oct. 29, 2019) (No. 3580010); Decision and Order on Motion at 2–3, Hoffman v. Stephenson, No. 650797/2019 (N.Y. Sup. Ct. June 24, 2019) (No. 89) (involving issuer defendant AT&T Inc.); Decision and Order at 7–12, *In re* PPDAI Grp. Sec. Litig., No. 654482/2018 (N.Y. Sup. Ct. July 5, 2019) (No. 91); Order Denying Venator and Huntsman Defendants' Motion to Stay Under Doctrine of Comity at 1, Macomb Cty. Emps. Ret. Sys. v. Venator Materials PLC, No. DC-19-02030 (Tex. Dist. Ct. Sept. 3, 2019).

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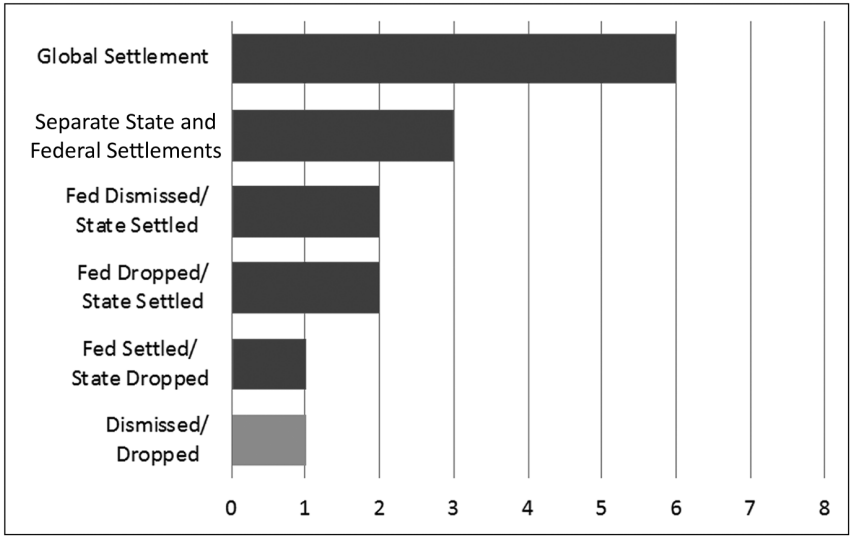
four pairs were dismissed or dropped. In two of those, the federal court dismissed its case while a stay was in effect in the state action, and the state court plaintiff thereafter dropped its case.[52] In one pair, both the federal and state courts granted motions to dismiss, and in the other pair both the federal and state action were voluntarily dropped—all while the stay of the state case was in effect. The remaining nine pairs of cases settled while the stays were in place.

There have been fifteen parallel pairs in which no stay was granted, either because no motion was made or because a motion was denied. Figure 6 shows the outcomes of these cases. There are a few instructive scenarios here. First, of the ten pairs where the federal case settled, nine of the federal cases included section 10 claims. The presence of section 10 claims in the federal case is an important factor in litigating parallel pairs of cases. Typically, at least one of those claims is

Figure 6
Outcomes of Parallel Pairs Where State Case Was Not Stayed



52. *See* Yan v. ReWalk Robotics Ltd., No. 17-cv-10169 (D. Mass. Jan. 31, 2017); *In re* ReWalk Robotics Ltd., No. 1684CV03336 (Mass. Super. Ct. Oct. 31, 2016) (showing that the federal motion to dismiss was granted in part and denied in part while state case was stayed, after which the state case was voluntarily dropped and ultimately dismissed); *see also* Altayyar v. Etsy, Inc., No. 15-cv-02785 (E.D.N.Y. filed May 13, 2015); Cervantes v. Allen & Company LLC, No. Civ534768 (Cal. Super. Ct. filed July 21, 2015) (involving issuer Etsy, Inc.) (showing a similar pattern in which the state court stayed the case on grounds of *forum non conveniens* which remained in effect until the federal case was dismissed, and thereafter the state case was dropped).

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based on alleged misstatements outside the defendant's offering documents. Consequently, the federal case includes one or more plaintiff classes in addition to the section 11 class (which is the same as the plaintiff class in the state case). Therefore, a settlement of the state case would have no impact on those section 10 claims in the federal case; the plaintiffs in the federal case would continue litigating those claims. On the other hand, because the federal case includes the state section 11 class (either in a section 11 claim or a section 10 claim based on the offering), a settlement of the federal case would end the entire litigation. Therefore, a defendant considering settlement of a parallel pair of cases in which the federal case has a section 10 claim based on statements or omissions outside the offering documents must focus primarily on the federal case to end the litigation. This is reflected in Figure 6. Five of the global settlements included federal cases with section 10 claims, as did all three of the separate state and federal settlements and the one pair where the federal case settled and the state case was dropped.

Second, there are two pairs where the state case settled and the federal case was dismissed. In one of these instances, the federal case had only a section 11 claim, which the federal court dismissed first. The state court then denied the defendant's motion to dismiss the section 11 claim—presumably because of a lenient state pleading standard—and the defendant had to settle the state case.[53] This is one of the troubling scenarios that litigation of parallel pairs of cases introduces. A defendant can go to the expense of having a federal complaint dismissed only to be forced to settle the state case after the state court denies the same motion.

Third, there are two parallel pairs where the state case settled and the federal case was dropped. In both those pairs, the state case settled before the federal court made a final ruling on a motion to dismiss. In one instance, the state court denied the defendants' motion to dismiss before a consolidated complaint was even filed in the federal case,[54] which presumably put pressure on the defendants to settle the state case. This too is a troubling scenario in that the state case drove up the defendants' litigation expense before the federal court ruled on a motion to dismiss.

The other instance in which a state case settled and a federal case was dropped is more ambiguous from the perspective of the defendant but not from a policy perspective. In that pair of cases, the initial federal complaint had been dismissed without prejudice.[55] The defendant then reached a settlement with the state plaintiff before the federal plaintiff filed an amended complaint. Although an outsider never knows what goes on in settlement negotiations, the defendant

53. *See* Greenberg v. Sunrun Inc., No. 3:16-cv-02480 (N.D. Cal. filed May 6, 2016); Pytel v. Elmore, No. CIV538215 (Cal. Super. Ct. filed Apr. 13, 2016) (involving issuer defendant Sunrun, Inc.). In the other instance of a federal court dismissal and a state court settlement, the federal case had only a section 10 claim, which is much harder for plaintiffs to plead successfully. Gregory v. ProNAi Therapeutics, Inc., No. 16-cv-08703 (S.D.N.Y. filed Nov. 9, 2016); Book v. Pronai Therapeutics, Inc., No. 16CIV02473 (Cal. Super. Ct. filed Nov. 18, 2016).

54. *See* Thomas v. Envivio, Inc., No. 3:12-cv-06464 (N.D. Cal. filed Dec. 20, 2012); Wiley v. Envivio, Inc., No. CIV517185 (Cal. Super. Ct. filed Oct. 5, 2012).

55. *See* Primo v. Pac. Biosciences of Cal., Inc., No. 11-cv-06599 (N.D. Cal. filed Dec. 21, 2011); Young v. Pac. Biosciences of Cal., Inc., No. CIV509210 (Cal. Super. Ct. filed Oct. 21, 2011).

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may in effect have run a reverse auction between the state and federal plaintiffs and taken the lowest settlement bid to end the litigation. On the other hand, if the defendant did not have to litigate the state and federal cases simultaneously, it might well have preferred to litigate the federal case at least through the pleading stage. From a policy perspective, having a judicial evaluation of a complaint and motion to dismiss is probably better than having two plaintiffs' attorneys bid on a settlement—if that is in fact what occurred.

These last two pairs of parallel cases bring us back to the possibility of staying a state case while litigating the federal case, at least up to the point of the federal court's final ruling on a motion to dismiss. In both those pairs, a stay of the state case pending resolution of the federal case would have been a better way to manage the litigation from a policy perspective and—at least in the first pair—from the perspective of the defendant.

State court stays pending a parallel federal case are thus a potentially useful tool with which to reduce redundant litigation and enhance judicial efficiency. Some courts have granted these stays and some have denied them. In explaining denials of these motions, some courts have relied on the presence of a section 10(b) claim in the federal case. The logic of this position is not compelling. So long as the federal case includes a section 11 claim as well, a settlement of that claim, which necessarily will mean certification of the section 11 class, will terminate the state case. A dismissal of a section 11 claim in the federal case will not terminate the state case (because the class will not have been certified), but that is unrelated to the presence of a section 10(b) claim.

Another potential tool with which a defendant might stop or at least slow down two-track litigation is to ask the federal court to stay state court discovery under section 27(b)(4) of SLUSA, which provides that "a court may stay discovery proceedings in any private action in a State court as necessary in aid of its jurisdiction."[56] Only a few defendants have moved for such a stay, and none of those motions have been granted.[57] In addressing these SLUSA-based motions to stay discovery in a parallel state case, the federal courts have been solely concerned with the possibility of cross-discovery—that the federal plaintiffs' lawyers will gain access to documents and testimony obtained in state court discovery before the federal parties are allowed to proceed with their own discovery. While the courts have acknowledged this possibility, they have been satisfied that it will not occur because the plaintiffs' lawyers in the state case are different from those in the federal case and because the state court has issued a protective order prohibiting disclosure of any information obtained during discovery. The federal courts have apparently not deemed it problematic that the defendant must bear the cost of state court discovery early in the proceedings, even though

56. 15 U.S.C. § 77z-1(b)(4) (2018) ("Upon a proper showing, a court may stay discovery proceedings in any private action in a State court as necessary in aid of its jurisdiction, or to protect or effectuate its judgments, in an action subject to a stay of discovery pursuant to this subsection.").

57. *See, e.g.*, Order Denying Motion to Stay State-Court Discovery at 3, Greenberg v. Sunrun Inc., No. 3:16-cv-02480 (N.D. Cal. May 1, 2017) (No. 93); Order at 1, Sommer v. comScore, Inc., No. 16-cv-01820 (S.D.N.Y. Oct. 27, 2016) (No. 137).

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this is what the PSLRA aimed to stop. Whether federal courts will be more willing to grant these motions as the volume of two-track litigation grows remains to be seen.

Conclusion

The data on section 11 litigation in state court show that concerns regarding the impact of the *Cyan* decision are well founded. Section 11 filings in state court have skyrocketed, and there is evidence to suggest that part of what is fueling these state filings are cases that are weaker than those filed in federal court. Equally troubling is the fact that close to half of post-*Cyan* litigation is now proceeding on parallel state and federal tracks. As a policy matter, this dual track litigation cannot be justified.

The ability of plaintiffs' lawyers to litigate section 11 cases without the encumbrance of the PSLRA's mandatory discovery stay and without the *Tombly–Iqbal* pleading standard is at the heart of both these problems. Plaintiffs' lawyers file cases in state court because the playing field there is attractive relative to that of federal court. A more lenient pleading standard coupled with early discovery may allow them to force a defendant to settle even a weak case. Furthermore, once a plaintiffs' lawyer files a case in state court, there is nothing to stop another lawyer from filing a parallel case in federal court. The cost of litigating two cases simultaneously further increases the pressure on defendants to settle. This is reflected in an 82 percent settlement rate where a defendant faces a parallel pair of cases.

There are some indications that state courts, most importantly in New York, will manage section 11 cases in ways that respond to these concerns. Some state courts have applied pleading standards specifically tailored to section 11 cases, some have stayed discovery until they rule on a motion to dismiss, and some have stayed their proceedings pending resolution of a parallel federal suit. But so far, these adjustments have been far from universal. In addition, unless a stay is ordered immediately upon the filing of a complaint—which has not yet occurred—these cases will not be litigated efficiently and pressure on defendants to settle will remain heightened.

The *Sciabacucchi* case may well provide a substantial measure of relief. Firms planning to go public or otherwise issue securities should certainly adopt a federal-forum provision and, if necessary, reincorporate in Delaware. There is no reason not to. But the effectiveness of a Delaware FFP will be known only after it is tested in the states in which plaintiffs file section 11 cases. At this point, those states are predominately New York and California, but if those states recognize FFPs as valid, plaintiffs' lawyers will likely test their validity in other states. Resolving the validity of FFPs, and the scope of their validity on an as-applied basis, will be a slow process as these cases proceed through multiple state courts. For firms that have already issued securities, but have not adopted an FFP, or that are not incorporated in Delaware, section 11 cases will continue to be litigated in state court as they have been since *Cyan*. Those firms could

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reincorporate in Delaware and adopt an FFP. It is unclear, however, whether an FFP will be upheld with respect to previously issued securities. That is an as-applied question state courts will have to decide.

Therefore, congressional intervention seems warranted. Although the Securities Act gave state courts jurisdiction to litigate section 11 cases from the start, the objective—if not the language—of SLUSA certainly appeared to be to shift jurisdiction exclusively to the federal courts. The most straightforward congressional intervention at this point would be to do just that—withdraw jurisdiction from state courts.

Might there be effective halfway measures Congress could adopt? There are some, but they would not solve the problem of costly and duplicative parallel litigation in state and federal court. Congress could enact a law providing that the PSLRA's discovery stay applies in state court. As explained above, some state courts have interpreted the PSLRA as doing just that, but others disagree. Legislation that makes this clear would be helpful, but a discovery stay coupled with a lenient pleading standard in state court would still mean onerous litigation for defendants—at least relative to litigating in federal court. Congress could also enact a heightened pleading standard to be applied in state courts and apply that standard to federal courts as well to avoid the possibility of different federal and state standards. This would go beyond what Congress did with respect to section 11 in the PSLRA, which applied a heightened pleading standard only to section 10(b) cases, but it is consistent with the concerns underlying that Act.

Addressing the problem of parallel litigation, however, can only be done by withdrawing state jurisdiction. One of the central reforms of the PSLRA was the rationalization of the consolidation process along with the selection of lead counsel and lead plaintiffs. That process replaced a race-to-the-courthouse regime in which plaintiffs' lawyers would attempt to get an inside track on becoming lead counsel by being the first to file a complaint. That regime was widely criticized as leading to the filing of non-meritorious lawsuits with little or no client oversight. Now, parallel litigation of section 11 cases potentially raises this problem again. First, there is no assurance that the selection of lead counsel and lead plaintiffs within each state will yield the best litigants. Second, there is no way to consolidate a state case with a federal case. Congress could provide that state courts shall immediately stay section 11 cases until a parallel federal case is resolved. This would be essentially a withdrawal of jurisdiction from the states where a parallel case in filed in federal court. But it would allow state courts to litigate cases where no parallel case is filed in federal court. If no plaintiffs' lawyer files a case in federal court, however, there is probably no good reason one should be filed in state court. Accordingly, the best reform would be to grant the federal courts exclusive jurisdiction over section 11 (and section 12) lawsuits.

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