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Commercial division update

Stays of state court securities actions: A changing tide?

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It is common for defendants facing parallel securities class actions in New York state court and federal court to seek a stay of the state proceedings. Historically, New York state courts have readily deferred to their federal counterparts, agreeing to stay the state action pending the outcome of the federal action, particularly in circumstances where the state complaint was less comprehensive. Two recent Commercial Division cases, however, suggest this approach may be changing, increasing the risk that securities defendants will face active, concurrent litigation in both state and federal court. This column explores these recent developments.

The *Cyan* Decision

In *Cyan, Inc. v, Beaver County Employees Retirement Fund*, 138 S. Ct. 1061, 1069 (2018), the U.S. Supreme Court considered whether the Securities Litigation Uniform Standards Act of 1998 ("SLUSA"), enacted in 1995, deprived state courts of subject matter jurisdiction over claims under the Securities Act of 1933 ("1933 Act"). Some courts had interpreted SLUSA to mandate exclusive federal court jurisdiction over the securities class actions asserting only 1933 Act claims, while others found concurrent jurisdiction.

The *Cyan* Court unanimously held that SLUSA does not deprive state courts of subject matter jurisdiction over 1933 Act claims, finding that "SLUSA's text, read most straightforwardly, leaves in place state courts' jurisdiction over 1933 Act claims, including when brought in class actions," and that such state court actions were not removable to federal court. As a consequence, securities defendants now find themselves defending 1933 Act cases in both state court and federal courts, as well as claims under the Securities Exchange Act of 1934 ("1934 Act") based on the same, or similar, allegations.

Commercial Division Decisions

In *Hoffman v. AT&T Inc.*, 2019 N.Y. Slip Op. 31811(U) (N.Y. Co., June 21, 2019), Justice Barry R. Ostrager of the New York County Commercial Division denied a defense motion to stay that state court securities class action "in favor of a subsequently filed and unquestionably more comprehensive federal action." In that case, filed in February 2019, Hoffman sued on behalf of the former shareholders of Time Warner Inc., alleging violations of the 1933 Act in connection with the June 2018 acquisition of Time Warner by AT&T, Inc. Plaintiffs alleged that, to acquire Time Warner, AT&T issued 1.185 billion shares of stock, but failed to disclose a "serious

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deterioration" in its DirecTV and DirecTV Now business. Two months later, in April 2019, other former Time Warner shareholders filed a complaint in the Southern District of New York asserting claims under both the 1933 Act and the 1934 Act. While the federal case arose from the same acts and omissions as the state court action, Justice Ostrager described the federal case as "assert[ing] broader claims on behalf of classes of variously situated Time Warner and AT&T shareholders."

In *Matter of PPDAI Group Sec. Litig.*, 2019 N.Y. Slip Op. 51075(U) (N.Y. Co. July 1, 2019), Justice Saliann Scarpulla of the New York County Commercial Division likewise denied a motion to stay that 1933 Act state action in favor of a parallel federal class action alleging claims under the 1933 Act and the 1934 Act. The plaintiffs' state court complaint, filed in September 2018, detailed allegedly misleading statements and omissions contained in securities offering materials in connection with an IPO of American Depository Shares by PPDAI Group, Inc. The federal case was filed in November 2018 in the Eastern District of New York by other shareholders based on allegations that were "virtually the same" as the allegations in the state court complaint.

Stay Rationale

Both *Hoffman* and *PPDAI* involved stay motions under CPLR § 2201, which provides that "[e]xcept where otherwise prescribed by law, the court in which an action is pending may grant a stay of proceedings in a proper case, upon such terms as may be just." In *PPDAI*, citing *Asher v. Abbott Laboratories*, 307 A.D. 2d 211, 211-212 (1st Dep't 2003), Justice Scarpulla set out the so-called *Asher* factors that a court may consider in determining whether to issue a stay, including:

> (1) which forum will offer a more complete disposition of the issues; (2) which forum has greater expertise in the type of matter; (3) which action was commenced first and the stage of the litigations; (4) whether there is substantial overlap between the issues raised in each court; (5) whether a stay will avert "duplication of effort and waste of judicial resources; and (6) whether plaintiffs have demonstrated that they would be prejudiced by a stay."

The court further noted that, when considering a motion to stay, New York courts often defer to the action that was first filed, citing *In re Topps Co., Inc. S'holder Litig.*, No. 600715/07, 2007 WL 5018882, at *3 (N.Y. Co. June 8, 2007) ("The general rule in New York is that 'the court which has first taken jurisdiction is the one in which the matter should be determined and it is a violation of the rules of comity to interfere" (citation omitted)). Being the first-filed case is not dispositive, however, Justice Scarpulla observed that New York courts generally restrain from applying this consideration mechanically, irrespective of other considerations. *AIG Fin. Prods. Corp. v. Penncara Energy, LLC*, 89 A.D.3d 495, 496 (1st Dep't 2011).

While Justice Ostrager in *Hoffman* did not directly address each of the Section 2201 factors, he noted New York state courts' historical approach had been to stay the state case in deference to the federal, including where the state action was first-filed, because state securities actions usually were less comprehensive than related federal actions, citing *Barron v Bluhdorn*, 68 A.D.2d. 809 (1st Dep't 1979). Justice Ostrager noted the rationale for this traditional approach was that "where there is a substantial overlap between the parties and issues and relief sought in both state and federal courts, staying the state court case would avoid the waste of judicial resources, potential inconsistent rulings, and duplication of effort," including because "federal courts have been perceived to have greater familiarity with securities laws."

Application of *Cyan*

In denying the requested stay in *Hoffman*, Justice Ostrager relied upon *Cyan* noting that the "first to file" rule in New York "must have some vitality in a post-*Cyan* world," with *Cyan* opening the door for plaintiffs to litigate securities actions in both state and federal forums. More importantly, Justice Ostrager emphasized the specialized nature of Commercial Division courts, noting that because of "the creation of specialized commercial courts in New York, the reasoning of the *Barron* case cannot be mechanically applied." In determining that this rationale is no longer relevant, the court stated that the issues presented in securities class actions are "less complex than issues the Commercial Division resolves every week," with the court expressing a strong view that "there is no reason to believe that the merits of plaintiff's claims cannot be resolved as efficiently and, perhaps, more expeditiously than the 1933 Act claims asserted in the federal action . . . ." The court went so far as stating that "because the federal action involves broader issues and multiple classes of shareholders, the federal court may consider staying the 1933 Act claims in the federal action in favor of this earlier filed action."

In *PPDAI*, Justice Scarpulla took a somewhat different approach, addressing each of the *Asher* stay factors in determining that the requested stay should be denied. The court found that there was no complete identity of parties between the state and federal action and that the issues did not substantially overlap, particularly as defendants argued that the 1933 Act claim in the federal case was time-barred. The fact that the state action was filed first strongly favored denial of a stay, the court predicating this conclusion on both the *Cyan* and *Hoffman* decisions (observing that if the first file rule were abandoned, New York courts would never exercise their jurisdiction to resolve first-filed 1933 Act claims, rendering *Cyan* meaningless.) The court cited *Hoffman* in finding that pre-*Cyan* cases cited by the movants were irrelevant to this determination, and agreed with Justice Ostrager that the Commercial Division's existence as a "specialized business court which deals exclusively with complex commercial litigation" supported denying a stay.

Finally, the court did not find defendants' arguments regarding duplication of effort persuasive, noting that the possibility of "two trials is not an appropriate basis for granting a stay."

Conclusion

The decisions in *Hoffman* and *PPDAI* indicate a possible shift by the Commercial Division towards less deference to the federal forum in securities class actions asserting claims under the 1933 Act. The decisions also reflect the confidence the Commercial Division's justices have that their expertise to hear complex securities class actions is equal to that of their federal counterparts. In any event, the CPLR § 2201 *Asher* factors will no doubt continue to be carefully analyzed and applied, including overlaps between parties and issues. Another major consideration will likely continue to be which action was filed first.

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