No. 20-1541

IN THE

Supreme Court of the United States

PIVOTAL SOFTWARE, INC., ET AL., *Petitioners*,
v.
ZHUNG TRAN, ET AL., *Respondents.*

ON PETITION FOR A WRIT OF CERTIORARI
TO THE COURT OF APPEAL FOR THE STATE OF
CALIFORNIA, FIRST APPELLATE DISTRICT

AMICUS CURIAE **BRIEF OF THE CHAMBER OF COMMERCE OF THE UNITED STATES OF AMERICA AND THE SECURITIES INDUSTRY AND FINANCIAL MARKETS ASSOCIATION IN SUPPORT OF PETITIONERS**

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INTERESTS OF AMICI CURIAE[1]

The Chamber is the world's largest business federation. It represents approximately 300,000 direct members and indirectly represents the interests of more than three million companies and professional organizations of every size, in every industry sector, and from every region of the country. An important function of the Chamber is to represent the interests of its members in matters before Congress, the Executive Branch, and the courts. To that end, the Chamber regularly files *amicus curiae* briefs in cases that raise issues of concern to the nation's business community. Many of the Chamber's members have sold or will in the future sell stock to the public through offerings governed by the Securities Act of 1933 (the "Securities Act") and will be directly affected by the application of the laws at issue in this case.

The Securities Industry and Financial Markets Association ("SIFMA") brings together the shared interests of hundreds of securities firms, banks, and asset managers. SIFMA's mission is to support a strong financial industry, investor opportunity, capital formation, job creation, and economic growth,

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[1] Pursuant to this Court's Rule 37.2(a), counsel of record for all parties consented to the filing of this *amicus curiae* brief. The ten-day notice period set forth in Rule 37.2(a) is not applicable because the Chamber and SIFMA (the "Amici") are filing earlier than ten days before the due date. This brief was not authored in whole or in part by counsel for any party, and no person or entity other than the Amici, their members, or their counsel made a monetary contribution intended to fund the preparation or submission of this brief.

while building trust and confidence in the financial markets. SIFMA, with offices in New York and Washington, D.C., is the U.S. regional member of the Global Financial Markets Association. Many of SIFMA's members serve as underwriters for, or otherwise participate in, securities offerings governed by the Securities Act and will be directly affected by the application of the laws at issue in this case. SIFMA regularly files *amicus curiae* briefs in cases with broad implications for the financial markets.

INTRODUCTION AND SUMMARY OF ARGUMENT

In 1995, Congress enacted the Private Securities Litigation Reform Act (the "Reform Act") to curb abusive securities class action litigation that "was being used to injure the entire U.S. economy." *Merrill Lynch, Pierce, Fenner & Smith Inc. v. Dabit*, 547 U.S. 71, 81 (2006) (internal quotation marks omitted). The Reform Act implemented a number of safeguards to address "those suits whose nuisance value outweighs their merits." *Id.* at 82. One of the most important safeguards created by the Reform Act is the discovery stay – in a securities class action, all discovery is automatically stayed until the court rules on the sufficiency of the complaint and determines that the plaintiff has stated a viable cause of action. *See* 15 U.S.C. § 77z-1(b)(1).

The Reform Act discovery stay was not an afterthought or corollary: it was a centerpiece of the legislation. The stay serves two critical functions in protecting issuer and underwriter defendants from meritless litigation. First, "[t]he cost of discovery often forces innocent parties to settle frivolous securities class actions." H.R. Rep. No. 104-369, at

37 (1995); *accord In re LaBranche Sec. Litig.*, 333 F. Supp. 2d 178, 181 (S.D.N.Y. 2004) ("The legislative history of the Reform Act indicates that Congress enacted the discovery stay to prevent plaintiffs from filing securities class actions with the intent of using the discovery process to force a coercive settlement."). Second, Congress intended to stop plaintiffs from using a meritless lawsuit to "conduct discovery in the hopes of finding a sustainable claim not alleged in the complaint." S. Rep. No. 104-98, at 15 (1995) ("Accordingly, the Committee has determined that discovery should be permitted in securities class actions only after the court has sustained the legal sufficiency of the complaint."). Congress' goals in adopting the Reform Act discovery stay apply with full force regardless of whether a securities class action is filed in state or federal court.

State courts that decline to apply the Reform Act discovery stay create substantial risks for securities class action litigation and the capital markets. By not applying the Reform Act discovery stay, state courts create judicial inconsistencies, allow plaintiffs with weak claims to fish for support through early discovery, and incentivize forum shopping for claims brought under the Securities Act. Collectively, these factors increase the risk and thus the costs that issuers and underwriters face when taking part in the IPO market.[2] And, by allowing discovery prior to

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[2] While this brief focuses on the Amici's affected members (issuers and underwriters), note that the Reform Act's discovery stay also provides important protection for public company officers and directors and auditors who are also regularly named as defendants in Securities Act class actions.

a finding that the plaintiff has stated a viable Securities Act claim, these state courts force issuer and underwriter defendants to spend millions of dollars and months, if not years, of effort on the discovery process in cases where the complaint ultimately may be found not to satisfy threshold pleading requirements.

For these reasons, the Amici respectfully request that this Court grant the Petition and find that the Reform Act automatic discovery stay applies to Securities Act claims brought in state court.

ARGUMENT

I. THE LOWER COURT ERRED IN DECLINING TO APPLY THE REFORM ACT AUTOMATIC DISCOVERY STAY TO SECURITIES ACT CLAIMS BROUGHT IN STATE COURT.

The California trial court erred in declining to apply the Reform Act discovery stay. The plain language of the Reform Act stays discovery during the pendency of a motion to dismiss in "any private action arising under" the Securities Act. 15 U.S.C. § 77z-1(b)(1). The Reform Act does not limit the stay to Securities Act cases filed in federal court, and actions brought in state court under the Securities Act plainly "arise under" the Act. *See Christianson v. Colt Indus. Operating Corp.*, 486 U.S. 800, 808 (1988) (a case arises under federal law when "federal law creates the cause of action"). Furthermore, as compared to several other provisions in § 77z-1, this provision is notably not restricted to actions brought "pursuant to the Federal Rules of Civil Procedure." *Compare* § 77z-1(b)(1) *with* § 77z-1(a)(1).

Moreover, reading the text to apply only in federal court would not make any logical sense given

Congress' goals of curbing abusive securities litigation and settlements driven by the costs and burdens of class action discovery. The only exception to the discovery stay is that a court may allow discovery if the court finds, "upon the motion of any party, that particularized discovery is necessary to preserve evidence or to prevent undue prejudice to that party." 15 U.S.C. § 77z-1(b)(1). It is critical that this Court grant the Petition so that it can correct the error of the California trial court and ensure that the Reform Act is being applied consistently and correctly to "any private action" filed under the Securities Act, not just those filed in federal court.

II. THIS COURT SHOULD GRANT THE PETITION BECAUSE STATE COURTS ARE APPLYING THE REFORM ACT DISCOVERY STAY INCONSISTENTLY.

At present, whether an issuer or underwriter defendant in a Securities Act case must bear the costs and burdens of discovery prior to the resolution of its pleading challenge is based solely on where the plaintiff chooses to file the complaint and which judge is assigned the case. There is no appellate authority on the application of the Reform Act discovery stay in state court, and little reason to believe there ever will be. In that vacuum, trial courts have fractured.

This split is evident from the published trial court opinions. For example, three different judges in the same New York county considered this question and reached three different results. *Compare Greensky, Inc. Sec. Litig.*, No. 655626, 2019 WL 6310525, at *1 (N.Y. Sup. Ct. Nov. 25, 2019) (finding stay inapplicable "by its terms" but staying discovery "to

give effect to the Reform Act's policy of staying discovery until a plaintiff has demonstrated that its 1933 Act claims have merit") *with Matter of Everquote, Inc. Sec. Litig.*, 65 Misc. 3d 226 (N.Y. Sup. Ct. 2019) (applying Reform Act stay), *and Matter of PPDAI Group Sec. Litig.*, 64 Misc. 3d 1208(A), at *7 (N.Y. Sup. Ct. 2019) (unpublished table decision) (finding stay inapplicable). Trial courts in other states have split along similar lines. *See Greensky*, 2019 WL 6310525, at *1 (collecting cases from California, Connecticut, and New York).

But these published opinions only scratch the surface of the split. There have been nearly 150 Securities Act cases filed in state court since 2011,[3] yet there are only a handful of reported opinions addressing the application of the Reform Act discovery stay. This small body of published case law is misleading and undersells both the extent of the split among state courts as well as the frequency with which the issue arises while evading appellate review.

Trial courts frequently decide requests to apply or reject the Reform Act discovery stay in oral rulings or in short form rulings without reasoned written opinions. And, even when trial courts do issue a written opinion on the issue, those opinions often go unpublished and may not be collected into any major database. *See, e.g.*, *State Trial Courts and Their Reporters*, DePaul Rinn Law Library, https://libguides.depaul.edu/c.php?g=253629

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[3] Michael Klausner, *State Section 11 Litigation in the Post-Cyan Environment (Despite Sciabacucchi)*, 75 The Business Lawyer 1769, 1775 (2020).

(updated Apr. 29, 2021) (noting trend in most states of not formally publishing trial court materials); *Published Trial Court Opinions*, Mass.gov, https://www.mass.gov/published-trial-court-opinions (last visited May 7, 2021) ("Most Trial Court opinions are not published at all."). As a result, many of the diverging trial court decisions on the application of the Reform Act discovery stay are unavailable to anyone but the litigants in a given case.

The situation is even worse at the appellate level. While appellate review is urgently needed to address this disarray, the state appellate courts have not issued even a single reasoned decision on this vital topic. Instead, they have simply denied mandamus without comment – a practice that is not unusual for mandamus petitions of all kinds in state court systems. *See, e.g.*, Judicial Council of Cal., *2020 Court Statistics Rep. Statewide Caseload Trends*, p. 3 (2020), https://www.courts.ca.gov/documents/2020-Court-Statistics-Report.pdf (reporting that 5,559 of the 5,875 original proceedings filed in California appeals courts in fiscal year 2018–19, or 94.6%, were disposed of without written opinion).

This matter illustrates the difficulty of obtaining (a) appellate review of a Reform Act discovery stay issue, and (b) a published body of case law that can lead to consensus among state courts. Here, the San Francisco Superior Court initially addressed the request of Pivotal Software, Inc. ("Pivotal") in a single sentence in its Order After October 27, 2020 Case Management Conference. It was only after Pivotal pressed the issue, by filing a writ of mandate with the appeals court and then a separate motion in the trial court, that the trial court explained its reasoning for denying the stay. Yet that explanation

was not published, and is currently unavailable in the major legal databases. And the appellate court did not even do that much, denying Pivotal's request in a one-sentence order.

This Court, and only this Court, is in a position to ensure the consistent and correct application of federal law to all cases brought under the Securities Act, regardless of forum.

III. FAILING TO APPLY THE REFORM ACT DISCOVERY STAY IN STATE COURT WILL ADVERSELY AFFECT THE CAPITAL MARKETS.

A. Capital Market Participants Face Increased Risks Due to Inconsistent Application of the Securities Act.

With state courts in key jurisdictions such as California and New York declining to apply the Reform Act discovery stay, there is an inconsistent application of the Securities Act in courts across the country. This inconsistency creates additional risk and uncertainty for issuers and underwriters participating in IPOs. As a result, underwriters may charge issuers increased fees to compensate for the additional risk of having to defend Securities Act cases without the benefit of the Reform Act discovery stay.

This concern is exemplified by the case at hand. Here, Pivotal was subject to parallel litigation in both state and federal court in California. In both instances, Pivotal sought dismissal of the claims for failure to state a claim. The federal case against Pivotal was dismissed months ago. In the state case, however, the trial court has not yet ruled on Pivotal's dismissal effort. Yet plaintiffs are seeking expansive and expensive discovery from Pivotal, the

Underwriter Petitioners,[4] and Dell, even though a federal court already has determined that the federal plaintiffs failed to plead a plausible Securities Act claim.

At best, Defendants will spend significant amounts of time and money engaging in discovery until the state court dismisses the action against Defendants. At worst, Plaintiffs will be able to coerce a windfall settlement or cherry-pick soundbites from documents obtained in discovery to attempt to bolster their meritless claims, thereby circumventing the core purpose of the Reform Act. To minimize the risks and costs caused by frivolous securities litigation, Congress required class action plaintiffs to plead facts establishing viable securities law violations **before** any discovery can begin.

Both of these results are exactly what Congress sought to avoid in including a discovery stay in the Reform Act, and both create unnecessary conflict between state and federal courts adjudicating the exact same claims.

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[4] The Underwriter Petitioners are Morgan Stanley & Co. LLC; Goldman Sachs & Co. LLC; Citigroup Global Markets Inc.; Merrill Lynch, Pierce, Fenner & Smith Inc.; Barclays Capital Inc.; Credit Suisse Securities (USA), LLC; RBC Capital Markets, LLC; UBS Securities LLC; Wells Fargo Securities LLC; KeyBanc Capital Markets Inc.; William Blair & Company, L.L.C.; Mischler Financial Group, Inc.; Samuel A. Ramirez & Co., Inc.; Siebert Cisneros Shank & Co., LLC; and Williams Capital Group, L.P.

B. Early, Unwarranted Discovery Will Force Windfall Settlements for Plaintiffs.

By declining to apply the Reform Act discovery stay, state courts have altered the incentives surrounding litigation and settlement of Securities Act cases. One of the reasons that Congress chose to implement the Reform Act was to avoid "extortionate settlements." *Dabit*, 547 U.S. at 81; *accord* H.R. Rep. No. 104-369, at 31 (1995) (noting that plaintiffs "abuse[d] . . . the discovery process to impose costs so burdensome that it [was] often economical for the victimized party to settle"). Declining to apply the Reform Act discovery stay in state court will subject the defendants sued in state court to the same abuses that the Reform Act sought to curb over 25 years ago.

Even prior to this Court's decision in *Cyan, Inc. v. Beaver County Employees Retirement Fund*, 138 S. Ct. 1061 (2018), which confirmed that state courts have jurisdiction over Securities Act claims, state court cases alleging Section 11 claims already were settling for higher amounts than comparable cases filed in federal court. *See* Joseph Grundfest, Sasha Aganin and Joseph Schertler, *After Cyan: Potential Trends in Section 11 Litigation*, LAW360 (Mar. 27, 2018), https://www.law360.com/articles/1026323/after-cyan-potential-trends-in-section-11-litigation. For example, from 2011 to 2015, the median settlement amount for Section 11 claims filed in California state court was more than twice the median settlement amount in federal court. *Id.*

Adding the cost and uncertainty of early discovery will only exacerbate the issue, returning to the pre-Reform Act days of "extortionate" settlement

risk. The cost of discovery – coupled with the risk of exposing the defendants to additional liability if plaintiffs are permitted to conduct fishing expeditions into emails, texts, chats, drafts, and other documents – may cause the defendants to settle for higher sums that are unrelated to the actual merits of the case. In contrast, settlements are lower in courts that enforce the Reform Act discovery stay, where the burden, as mandated by the Reform Act, is on the plaintiff to demonstrate that it has a viable claim without the benefit of early discovery. Thus, the outcome (settlement versus litigation) of two identical cases, one in federal court and one in state court, may be driven solely by the forum in which it is filed, a result that is neither contemplated by the Reform Act nor by principles of equality, consistency, and judicial efficiency.

C. The Adverse Effects of Early Discovery in State Court Are Magnified By Rampant Forum Shopping.

Because the Securities Act's jurisdictional provision permits plaintiffs to file in state or federal court nationwide, IPO participants may be increasingly dragged into litigation in discovery-friendly forums regardless of whether there is a substantial connection between the case and that forum. Courts generally seek to avoid forum shopping,[5] and courts have recognized that failing to apply a rule of decision, like the Reform Act, that

[5] *Cf. Beeman v. Anthem Prescription Mgmt., LLC*, 58 Cal. 4th 329, 340 (2013) (answering certified question to avoid the inevitable forum shopping that would result from a law being enforceable in federal, but not state, courts).

establishes a clear and consistent federal policy "invite[s] forum shopping by creative lawyers" which "could have a negative impact on the courts" and damage the uniform federal policy. *Webb v. Superior Ct.*, 225 Cal. App. 3d 990, 1000 (Ct. App. 1990); *see also Agency Holding Corp. v. Malley-Duff & Assocs., Inc.*, 483 U.S. 143, 154–56 (1987) (finding need for uniform civil RICO statute of limitations to promote consistent application of the law and discourage forum shopping).

Forum shopping is an acute risk in the Securities Act context because it has a broad jurisdictional provision. The Securities Act provides for jurisdiction "in the district wherein the defendant is found or is an inhabitant or transacts business, or in the district where the offer or sale took place, if the defendant participated therein, and process in such cases may be served in any other district of which the defendant is an inhabitant or wherever the defendant may be found." 15 U.S.C. § 77v. Most public companies and large banks do business in most, if not all, U.S. states, potentially subjecting them to jurisdiction under the Securities Act in most U.S. jurisdictions, not just where the entity is incorporated or headquartered. And, setting aside the issue of personal jurisdiction, this Court recently reaffirmed state courts' "longstanding jurisdiction to adjudicate class actions alleging only 1933 Act violations." *Cyan*, 138 S. Ct. at 1078.

Based on the filing statistics related to Securities Act claims, plaintiffs already have begun to concentrate their filings in those jurisdictions where they may gain access to pre-motion discovery. For example, from 2011 to 2017, before the *Cyan* decision, an average of 9.28 Securities Act cases were

filed in state courts per year. *See* Klausner, *supra*, at 1775. Then, after *Cyan*, from 2018 to 2019, the average spiked to 38.5 cases a year. *Id.*[6] Across the country, 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." *Id.* at 1776.

The statistics reveal another issue – an increase in parallel and duplicative state and federal court cases. *See Seneca Ins. Co., Inc. v. Strange Land, Inc.*, 862 F.3d 835, 846 (9th Cir. 2017) (noting that improper forum shopping includes seeking "more favorable rules in [plaintiff's] choice of forum or pursu[ing] suit in a new forum after facing setbacks in the original proceeding"). From 2011 to 2013, only 7% of Securities Act claims were brought in both state and federal court, and, from 2014 until March 20, 2018, when *Cyan* was decided, the number of parallel suits grew to only 17% of Securities Act claims. Klausner, *supra*, at 1775. In sharp contrast, 49% of all Securities Act claims filed between March 21, 2018 and December 31, 2019 were filed in both state and federal court. *Id.* At the same time, Securities Act cases filed exclusively in federal court

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[6] While Securities Act filings dropped in 2020, the number of filings still did not return to pre-*Cyan* levels. The drop in filings is due to a number of factors, including the COVID-19 pandemic, which delayed many IPOs to the second half of 2020. Jessica Chen and John Vetterli, *Global IPOs Hit Back Strongly After COVID-19 Crash*, White & Case (Mar. 08 2021), https://www.whitecase.com/publications/insight/global-ipos-hit-back-strongly-after-covid-19-crash (noting that the first half of 2020 saw the lowest volume of IPOs in the last five years).

dropped from 88% between 2011 and 2013 and 65% between 2014 and March 20, 2018 to a mere 29% after March 21, 2018. *Id.*

Declining to apply the Reform Act discovery stay will draw plaintiffs to plaintiff-friendly state courts in disproportionate numbers, regardless of the plaintiffs' location or the location of the defendants. With an increasing risk of parallel litigation in multiple forums involving early discovery, many underwriters may demand increased fees from issuers to compensate for the new risk. Issuers themselves may seek alternatives, such as direct listings. Nicki Locker & Laurie Smilan, *Carving Out IPO Protections*, Harvard Law School Forum on Corporate Governance (Feb. 25, 2020), https://corpgov.law.harvard.edu/2020/02/25/carving-out-ipo-protections/. Without intervention from this Court, plaintiffs will continue to file parallel and duplicative Securities Act cases in a few hand-picked, plaintiff-friendly forums that will not apply the Reform Act discovery stay, creating undue burden on courts and litigants.

D. Declining to Apply the Discovery Stay Will Encourage the Filing of Weak and Meritless Lawsuits, Contrary to Congress' Intent.

Even before *Cyan* was decided, Plaintiffs already perceived certain state courts to be preferred places to file Securities Act claims because those state courts have dismissed claims at a lower rate in recent years. *See, e.g.*, Klausner, *supra*, at 1777 (finding dismissal rates of Section 11 cases in state courts of 28% compared to 39% for federal cases, and noting that in California from 2011 to 2019, only 18% of Section 11 cases had been dismissed).

After *Cyan* was decided, there was an overall increase in Section 11 cases that was not accompanied by an increase in the number of public offerings, which "suggests that the increases may have been driven by an increase in low-merit cases that are attracted to state courts . . . ." *Id.* at 1776.

Declining to apply the Reform Act discovery stay can only exacerbate this issue. Plaintiffs with weak claims will file where they are permitted to conduct early discovery, giving them an opportunity to force settlements or, failing that, a chance to try to survive a pleading challenge by amending their complaints with selective and cherry-picked excerpts from a defendant's emails or other documents (an opportunity not available to identically situated federal plaintiffs).

IV. STATE COURTS' DISREGARD OF THE REFORM ACT DISCOVERY STAY INCREASES THE BURDENS AND COSTS THAT THE REFORM ACT SOUGHT TO CURB.

As set out in Appendix A to Pivotal's application for a stay, since *Cyan* was decided, the Underwriter Petitioners "cumulatively have been named as defendants in individual and consolidated actions under the Securities Act in state court at least 287 times—or, counting the number of complaints filed within each individual and consolidated action, cumulatively at least 640 times." As repeat participants in the capital markets generally, and initial and secondary public offerings specifically, these banks will be regularly subject to expensive and expansive discovery if the Reform Act discovery stay is not applied to cases brought in state court.

Most public offerings, including large companies located in California and New York, are underwritten by multiple banks. Those banks, in turn, have indemnification agreements with the issuers that cover, among other things, the cost of defending securities class actions. Given these facts, a rule allowing discovery in state court Securities Act cases – before courts find that the complaints state a claim – risks compounding costs for issuer defendants as well.

In addition, the explosion of Securities Act cases in state court has cost market participants in other ways. For example, the cost of directors and officers insurance has **quadrupled** since *Cyan*. Priya Cherian Huskins, *Will D&O Insurance Rates End the IPO Party?*, Woodruff Sawyer (Jan. 15, 2020), https://woodruffsawyer.com/do-notebook/do-insurance-rates-ending-ipo-party/. Insurers are "chopping coverage limits and requiring IPO clients to pick up more costs before a policy kicks in," as well as "requiring companies to pay for a percentage of the eventual loss." Suzanne Barlyn, *D&O Insurance Costs Soar as Investors Run to Court Over IPOs*, Insurance Journal (June 18, 2019), https://www.insurancejournal.com/news/national/2019/06/18/529691.htm. Increased IPO costs already have caused issuers to look to other options for going public. *See, e.g.*, Locker & Smilan, *supra* (noting increased use of self-help strategies, direct listings, and carve-outs to IPO lock-up agreements). The use of these mechanisms reduces pressure on issuers to adopt governance reforms that protect investors, which undermines the ultimate purpose of the Securities Act. Brent J. Horton, *Spotify's Direct*

Listing: Is It a Recipe for Gatekeeper Failure? 72 SMU L. Rev. 177, 202–12 (2019).

If IPO costs remain high, or climb even higher, non-issuer participants may begin to feel the impact as well. Underwriters, consultants, and experts all may demand higher fees or other more favorable terms before they are willing to participate in an initial or secondary public offering.

CONCLUSION

For the foregoing reasons, the Amici respectfully request that this Court grant Pivotal's Petition and reverse the conclusion of the trial court that the Reform Act discovery stay does not apply in state court.

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