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# Litigation

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## PLAINTIFF'S MOTION TO REMAND 1933 ACT CLAIMS DENIED: COURT HOLDS ONLY FEDERAL COURTS HAVE JURISDICTION OVER SUCH CLAIMS

Class action plaintiffs bringing claims under the Securities Act of 1933 (the “Securities Act”) may have less of a choice between state and federal court than their pleadings assert. Plaintiffs commonly allege that their Securities Act claims are properly filed in state court and are not removable. However, in a recent decision from the Southern District of New York, *Knox v. Agria Corp.*, Judge William H. Pauley ruled that only federal courts have subject matter jurisdiction over Securities Act claims.<sup>1</sup>

Historically, Securities Act claims could be brought in either state or federal courts. In 1995, Congress enacted the Private Securities Litigation Reform Act (“PSLRA”), and in 1998, the Securities Litigation Uniform Standards Act (“SLUSA”). The goals of the PSLRA and SLUSA were to heighten the pleading standards for securities lawsuits and have such suits litigated in federal courts. In

SLUSA, Congress preempted many state law securities class actions and modified the removal provisions of the Securities Act. But the SLUSA amendments left open whether state courts retained concurrent jurisdiction over Securities Act claims. Different jurisdictions have answered this question differently. The recent *Agria* decision from the United States District Court for the Southern District of New York is good news for defendants, but does not (and cannot) definitely resolve the underlying debate.

### **The History of the Jurisdictional Provision of the Securities Act**

When first enacted, the Securities Act provided for federal jurisdiction “concurrent with State and Territorial courts, of all suits in equity and actions at law brought to enforce any liability or duty created by this title”<sup>2</sup> and stated that “no case ... brought in any State court of competent jurisdiction shall be removed

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<sup>1</sup> No. 08 Civ. 7651, 2009 U.S. Dist. LEXIS 6078 (S.D.N.Y. Jan. 27, 2009). The *Agria* complaint alleged that it was not removable. See Complaint ¶ 9.

<sup>2</sup> 15 U.S.C. § 77v (1994).

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to any court of the United States.”<sup>3</sup> After the PSLRA heightened the pleading requirements for securities fraud lawsuits, plaintiffs’ lawyers increasingly commenced securities fraud lawsuits in state courts.<sup>4</sup> This trend led to the passage of SLUSA in 1998. SLUSA amended the non-removal provision of the Securities Act and made it clear that securities fraud claims brought in state court under state statutory and common law could be removed. But, some found SLUSA’s language to be unclear as to whether suits encompassing *only* Securities Act claims could be removed to federal court. Not surprisingly, plaintiffs’ lawyers desirous of avoiding federal court began to file “pure” Securities Act class actions in state courts. The district courts are divided on whether such class actions can be removed,<sup>5</sup> and for a number of reasons, there has been (and is not likely to be) appellate authority to resolve that division.

<sup>3</sup> *Id.*

<sup>4</sup> See, e.g., Jordan A. Costa, Note, *Removal of Securities Act of 1933 Claims After SLUSA: What Congress Changed, and What it Left Alone*, 78 St. John’s L. Rev. 1193, 1201-04 (2004) (reviewing the intended and unintended consequences of PSLRA).

<sup>5</sup> Compare *Unschuld v. Tri-S Sec. Corp.*, No. 06 Civ. 2931-JEC, 2007 U.S. Dist. LEXIS 68513 (N.D. Ga. Sept. 14, 2007) (granting remand to state court); *Irra v. Lazard Ltd.*, 2006 WL 2375472 (E.D.N.Y. Aug. 15, 2006) (same); *Haw. Structural Ironworkers Pension Trust Fund v. Calpine Corp.*, No. 03-civ-0714-BTM (JFS), 2003 U.S. Dist. LEXIS 15832 (S.D. Cal. Aug. 26, 2003) (same); with *Rubin v. Pixelplus Co. Ltd.*, No. 06 Civ. 2964 (ERK), 2007 U.S. Dist. LEXIS 17671 (E.D.N.Y. Mar. 13, 2007) (denying remand); *Pinto v. Vonage Holdings Corp.*, No. 07-62, 2007 U.S. Dist. LEXIS 33287 (D.N.J. May 4, 2007) (same); *Brody v. Homestore, Inc.*, 240 F. Supp. 2d 1122 (C.D. Cal. 2003) (same).

### The *Knox v. Agria Corp.* Decision

In 2008, Knox filed a putative class action in New York Supreme Court asserting claims under the Securities Act. His complaint specifically alleged that the state court had subject matter jurisdiction and that his claims were not removeable. At the same time, three federal securities class actions against the same defendants were pending in the United States District Court for the Southern District of New York. Knox’s complaint contained allegations similar to those in the federal complaints. The defendants removed Knox’s action pursuant to 28 U.S.C. § 1441(a). Knox then filed a motion to remand.

The district court first addressed the anti-removal provision of the Securities Act, which states that “[e]xcept as provided in section [16(c)] of the [Securities Act], no case arising under the [Securities Act] and brought in any State court of competent jurisdiction shall be removed to any court of the United States.”<sup>6</sup> Therefore, state and federal courts have concurrent jurisdiction over Securities Act claims “except as provided in [Section 16] with respect to covered class actions.”<sup>7</sup> Section 16(c) provides that “[a]ny covered class action brought in any State court involving a covered security, as set forth in subsection (b), shall be removable to the Federal district court and shall be subject

to subsection (b).”<sup>8</sup> Subsection (b) prohibits state or federal courts from hearing any covered class action raising state or common law claims based on untrue statements or deceit in the sale of a nationally traded security.<sup>9</sup> A narrow reading of these sections would lead a court to conclude that Section 16(c) only applies to covered class actions raising state or common law claims, whereas a broad reading would allow district courts to construe Section 16(c) to include Securities Act claims.<sup>10</sup>

Judge Pauley adopted the broad reading and criticized courts that have remanded Securities Act claims because, among other things, it “creates a jurisdictional anomaly of prohibiting state securities fraud claims in state court, while allowing federal securities fraud class actions to be litigated there.”<sup>11</sup> Judge Pauley avoided construing the anti-removal provision by holding that SLUSA actually divested state courts of subject matter jurisdiction over covered class actions: “[b]ecause this Court holds that no state court has subject matter jurisdiction over covered class actions raising [Securities] Act claims, it need not address the scope of the exception to the anti-removal provision.”<sup>12</sup>

The jurisdictional provision of the Securities Act provides that “[t]he district courts of the United States shall have jurisdiction of offenses and violations under [the

<sup>8</sup> 15 U.S.C. § 77p(c).

<sup>9</sup> 15 U.S.C. § 77p(b).

<sup>10</sup> *Knox*, 2009 U.S. Dist. LEXIS 6078 at \*6-7.

<sup>11</sup> *Id.* at \*7.

<sup>12</sup> *Id.* at \*8.

<sup>6</sup> 15 U.S.C. § 77v(a).

<sup>7</sup> *Knox*, 2009 U.S. Dist. LEXIS 6078 at \*9 (quoting 15 U.S.C. § 77v(a)).

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Securities Act] and concurrent with State and Territorial courts, except as provided in [Section 16] with respect to covered class actions, of all suits in equity and actions at law brought to enforce any liability or duty created by the [Securities Act].”<sup>13</sup> Section 16 addresses covered class actions,<sup>14</sup> and the district court found that “the exception in the jurisdictional provision of Section 22(a) exempts covered class actions raising 1933 Act claims from concurrent jurisdiction.”<sup>15</sup> Under this view, because SLUSA stripped state courts of concurrent jurisdiction over covered class actions raising Securities Act claims, the anti-removal provision — the scope of which has been a key point of dispute in removal motions — becomes irrelevant.<sup>16</sup>

### The Future of Securities Act claims after the *Knox* Decision: Unclear

There is a significant split in authority on whether pure Securities Act class actions are removable. While some district courts have held that they are, other district courts have held the opposite.<sup>17</sup> No federal appellate court has addressed the issue, although the United States Court of Appeals for the Second

Circuit (arguably in *dicta*) stated that “Section 16(c) of the Act excepts ‘class action[s] brought in state court’ from the scope of the nonremoval provision and provides that those class actions ‘shall be removable to the Federal court for the district in which the action is pending.’”<sup>18</sup>

Absent action by Congress, it is possible that no clear answer is on the horizon. Although they can be persuasive authority, district court decisions are not binding on other judges even in the same district, and district judges are free to resolve legal questions like these unless there is controlling circuit or Supreme Court authority. For example, different judges in the United States District Court for the Eastern District of New York have granted and denied remand motions relating to “pure” Securities Act claims.<sup>19</sup>

Appellate courts are not likely to resolve this issue. Federal appellate courts can hear appeals from only final decisions, and denials of remand are not considered final. Review of a denial of remand must therefore be accomplished by mandamus or interlocutory appeal, (both of which have significant discretionary components) or be raised on direct appeal at the end of the case. Because most securities actions are dismissed or settled, it is difficult for the issue to come up to the circuit courts.

In addition, if a case *is* remanded, that decision is not reviewable on appeal.<sup>20</sup> Although there are potentially other ways to have this issue addressed by the federal appellate courts, to date no such case has been presented.

The conflicting holdings of the district courts, even courts within the same district, likely will give rise to continued forum shopping by plaintiffs. Plaintiffs will seek to file Securities Act claims in districts that have or might narrowly interpret the Securities Act’s jurisdictional provision. But until Congress gives clearer instruction on this issue, Judge Pauley’s decision in *Agria* strengthens the argument that state courts do not have subject matter jurisdiction to hear covered class actions raising Securities Act claims.

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<sup>13</sup> 15 U.S.C. § 77v(a).

<sup>14</sup> See 15 U.S.C. § 77b(f) (defining “covered class actions”).

<sup>15</sup> *Knox*, 2009 U.S. Dist. LEXIS 6078 at \*13.

<sup>16</sup> *Id.* (“This is what other courts have overlooked: because the anti-removal provision only applies to claims brought in a state court of competent jurisdiction, once SLUSA stripped state courts of subject matter jurisdiction over covered class actions raising 1933 Act claims, the reach of the anti-removal provision receded, leaving covered class actions raising 1933 Act claims *exclusively* for federal courts.”) (emphasis added).

<sup>17</sup> See *supra* note 5.

<sup>18</sup> *Cal. Pub. Employees’ Retirement Sys. v. WorldCom, Inc.*, 368 F.3d 86, 97 (2d Cir. 2004) (quoting 15 U.S.C. § 77p(c)) (emphasis in original).

<sup>19</sup> Compare *Irva v. Lazard Ltd.*, 2006 WL 2375472 (E.D.N.Y. Aug. 15, 2006) (granting remand) with *Rubin v. Pixelplus Co., Ltd.*, 2007 WL 778485 (E.D.N.Y. Mar. 13, 2007) (denying remand).

<sup>20</sup> See 28 U.S.C. § 1447(d) (“An order remanding a case to the State court from which it was removed is not reviewable on appeal or otherwise . . .”).

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