

## [Securities Regulation Daily Wrap Up, FEDERAL PREEMPTION—U.S.: Securities Act defendant argues PSLRA discovery stay applies in state court, \(Aug. 23, 2021\)](#)

Securities Regulation Daily Wrap Up

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By [Anne Sherry, J.D.](#)

Post-*Cyan*, increasing numbers of Securities Act suits are being brought in state court. The Supreme Court will decide if the PSLRA's stay of discovery during the pendency of a motion to dismiss applies to these actions.

In a brief filed with the U.S. Supreme Court, defendants in a private securities fraud case filed in state court argued that the PSLRA stays discovery in the action, rather than applying only to a private action in federal court, as the plaintiffs argue. The plain language of the PSLRA stay provision applies to "any private action" arising under the Securities Act, and Congress expressly limited other parts of the PSLRA to federal court when it saw fit, the defendants argue ([Pivotal Software, Inc. v. Superior Court of California, City and County of San Francisco](#), August 2021).

The question presented concerns Section 77z-1(b)(1) of the PSLRA, which provides, "In any private action arising under [the Securities Act of 1933], all discovery and other proceedings shall be stayed during the pendency of any motion to dismiss, unless 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."

The action at issue was filed in the California Superior Court, challenging statements made in a software company's IPO registration statement and bringing claims under Securities Act Sections 11, 12(a)(2), and 15. The trial court denied a motion to stay discovery after concluding that the PSLRA stay provision only applies in federal courts, in part due to the lack of express references to state courts in the text. The California appellate and Supreme Court both summarily denied relief, and the U.S. Supreme Court granted certiorari in its final order list of October Term 2020.

**Petition.** The petition argued that the plain language of the provision applies to any private action, just like it says, no matter if brought in state or federal court. The state trial courts, however, are split on the issue. Furthermore, more Securities Act claims are brought in state court since the Supreme Court held in *Cyan* (U.S. 2018) that state courts have concurrent jurisdiction over Securities Act claims. The issue, however, has consistently evaded appellate review since it arises during a stage not reviewable after final judgment and, moreover, the disputes and orders are often unreported. The petition said that since there is no viable path for appellate review of this question, the Court should take the opportunity to clarify the matter.

**Brief.** As did their petition, the petitioners' brief argues that the clear language of the PSLRA stay is simple in that it refers to "any private action arising under" the Securities Act. To hold that the stay does not apply in cases filed in state court would mean that it applies only to some actions, not "any" action. Furthermore, the PSLRA expressly states when its provisions are limited to actions in federal court. The broader application of the stay to "any private action" aligns with Congress's purpose to eliminate unnecessary discovery costs and preclude "fishing expeditions," the brief states.

The petitioners also assert that there was no basis for the state court to limit the discovery stay to cases brought in federal court, as a statute need not expressly identify state courts to apply there, and none of the PSLRA provisions on which the state court relied supports carving out state courts from the discovery stay. While *Cyan* described some of the PSLRA provisions that apply in state court as "substantive," the Court did not hold that their applicability in state court turned on this characteristic.

The petitioners also challenged the respondents' attempt to rely on the canon of constitutional avoidance, writing that this canon does not apply to an unambiguous statute and that the PSLRA provision raises no constitutional concerns. Congress has constitutional authority to regulate how state courts adjudicate federal claims, the brief asserts. Furthermore, there is no support in the legislative history to restrict the PSLRA stay to federal court. That history provides no basis to presume that Congress was unaware that state courts exercise concurrent jurisdiction over Securities Act suits or believed that its restrictions on discovery were not important enough to apply in state court.

The case is [No. 20-1541](#).

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Companies: Pivotal Software, Inc.; Morgan Stanley & Co. LLC; Goldman Sachs & Co. LLC

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