Removability of Federal Class Action Claims From State Court

For decades, the volume of securities class actions has grown. Initially most were filed in federal court, but the number of securities class actions filed in state court has increased steadily and in 2010 surpassed the number of federal court filings. Recognizing the “ways in which the class action device was being used to injure ‘the entire U.S. economy,’” Congress passed the Private Securities Litigation Reform Act (PSLRA) in 1995. The PSLRA, Pub. L. No. 104-67, 109 Stat. 737 (1995), introduced heightened procedural standards in federal court by: (1) limiting plaintiffs’ recovery of damages and attorney fees; (2) mandating a discovery stay until the resolution of any motion to dismiss; and (3) imposing heightened pleading requirements.

Because these heightened standards applied only to the federal securities laws, plaintiffs avoided them by bringing actions under state law. To address this trend, Congress passed the Securities Litigation Uniform Standards Act of 1998 (SLUSA), which precludes state and federal courts from hearing certain covered class actions brought under state law. As the U.S. Supreme Court recognized, Congress enacted SLUSA, Pub. L. No. 105-333, 112 Stat. 3230 (1998), “[t]o stem the ‘shift from Federal to State courts’ and ‘prevent certain State private securities class action lawsuits alleging fraud from being used to frustrate the objectives of the [PSLRA].’”

However, an apparent drafting error in SLUSA creates a loophole that (1) permits plaintiffs to file federal securities class actions in state court, and (2) prevents defendants from removing those actions to federal court.

Background

Under the original Securities Act of 1933 (1933 Act), 15 U.S.C. §77a, et seq., plaintiffs could file an action and remain in either state or federal court because the statute granted concurrent jurisdiction and prevented removal of 1933 Act claims from state to federal court. But after SLUSA, any “covered class action” as defined in SLUSA is removable to federal court.

In relevant part, 15 U.S.C. §77v(a) provides: The district courts of the United States and the United States courts of any Territory shall have jurisdiction of offenses and violations under this subchapter...and, concurrent with State and Territorial courts, except as provided in section [77p] of this title with respect to covered class actions, of all suits in equity and actions at law brought to enforce any liability or duty created by this subchapter... Except as provided in section [77(c)] of this title, no case arising under this subchapter and brought in any State court of competent jurisdiction shall be removed to any court of the United States. (emphasis added). SLUSA added the emphasized language. Notably, the statute’s definitions do not explain what claims must be alleged for a covered class action to be removable. Rather, Section 77(c), titled “Removal of Covered Class Actions,” provides that “any 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 for the district in which the action is pending, and shall be subject to subsection (b).” Subsection (b) provides that “no covered class action based upon the statutory or common law of any State or subdivision thereof may be maintained in any State or Federal court by any party alleging securities violations.” Subsection (b) therefore offers the only description of which class actions are removable, and on its face it limits removal to state law actions. SLUSA is otherwise silent on whether federal claims may be brought in state court or whether those claims are removable.

Subsection (b) is in tension with SLUSA’s legislative history, and courts are split over whether federal securities class action claims are removable from state court. Guidance from appellate courts is lacking because federal jurisprudence prohibits appellate review of a district court’s decision to remand. Notably, decisions denying remand of 1933 Act claims to state court under SLUSA have also escaped review. Inconsistent district court decisions exist both within and across the circuits. Without appellate clarification, there remains substantial uncertainty as to whether federal securities claims brought in state court must remain there.

Compounding the confusion is Supreme Court dicta cited by district courts in support of both remand and removal. In Kircher v. Putnam Funds Trust, the Supreme Court held that the remand of plaintiff’s state law claims was not reviewable on appeal. Although the court in Kircher addressed only removability of state law claims, the court interpreted the same two sections that govern the removability of 1933 Act class actions. The court explained that district courts’ subject matter jurisdiction depends on Section 77(p)(c), and removal under that provision is limited to cases set forth in subsection (b), “namely, those with claims of untruth, manipulation, and so on.” Whereas the
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Varying Approaches

District courts are split into three camps on this issue. On one side, district courts hold that SLUSA only permits removal of state law actions, thus barring removal of 1933 Act class actions. This narrow approach predominantly focuses on the plain language of SLUSA as supported by Kircher. Courts employing this approach emphasize that the removal provision, Section 77p(c), incorporates reference to subsection (b), which is limited to covered class actions “based upon the statutory or common law of any State,” and thus 1933 Act claims are not removable.

Although some courts argue that SLUSA’s legislative history supports the narrow position, others acknowledge that Congress evinced intent to authorize removal of all covered class actions, including 1933 Act claims, but feel bound by the statutory language. As one court explained, “where the language of the statute is clear, it is not up to the Court to modify it to effect Congress’s likely intent.” At the opposite extreme, courts employ a broad approach, focusing on legislative intent over statutory language. SLUSA’s congressional findings state that before enactment, “considerable evidence [was] presented...that a number of securities class action lawsuits...shifted from Federal to State courts [and that] shift...prevented [the] Act from fully achieving its objectives.” As one court stated, the interpretation “that SLUSA meant to authorize removal of securities litigation brought pursuant to state law—is simply irreconcilable with [the statute’s intent].” Nonetheless, for this broad approach, courts must ignore the intuitive reading of the statute (i.e., that Section 77p(b) must be read into Section 77p(c)).

Instead, those courts reason that removability better harmonizes Section 77p(c), which “does not contain an explicit limitation on actions that are removable,” with Section 77v(a), which “plainly provides for the exercise of jurisdiction by federal courts and the removal of actions brought ‘under this subchapter,’” namely, the Securities Act. As emphasized in Rubin v. Pixelplus C, an Eastern District of New York case, finding 1933 Act claims not removable “would lead to an absurd result that would undermine the principal purpose of SLUSA, which was to stop ‘state-court litigation of class actions involving nationally traded securities.’

A third “jurisdictional” approach supporting removability was pioneered by the Southern District of New York in Knox v. Agria Corp. and adopted by the Northern District of California in Lapin v. Facebook. To resolve the conflict between SLUSA’s language and its intent, the Knox court analyzed the removability problem from the lens of SLUSA’s jurisdictional provision (Section 77v(a)), instead of its removal provision (Section 77p(c)). The jurisdictional provision states that federal and state courts have concurrent jurisdiction over 1933 Act claims, “except as provided in section [77p]...with respect to class actions.” According to Knox, the phrase “except as provided” modified SLUSA’s general grant of concurrent jurisdiction and stripped state courts of the power to adjudicate any federal class qualifying as a “covered class action” under Section 77p(b) of the 1933 Act. However, this analysis ignores another modifying phrase in Section 77v(a), namely “except as provided in subsection (b),” which contemplates only claims based in state law. Even under the jurisdictional approach, a plain text reading of SLUSA indicates that concurrent jurisdiction remains over federal claims, leaving unanswered the scope of the removability provision.

Conclusion

Decisions interpreting SLUSA’s removal provision range from narrow interpretations contrary to the clear statutory intent to high-level views or tortured readings focused on the statute’s overall purpose. The Supreme Court in Kircher arguably advocated a result at odds with SLUSA’s overall purpose, stranding 1933 Act claims in state courts. And district courts continue to twist Kircher into support for both remand and removability of 1933 Act claims. Because of the limited judicial review available and the corresponding lack of appellate court guidance, legislative action is needed to tie up this loophole and clear the uncertainty as to whether SLUSA requires federal securities actions to be heard in federal court.

11. 28 U.S.C. §1447(d) (limiting appellate review of all district court decisions to remand, except when removal is pursuant to 28 U.S.C. §1444(c)).
13. Id.
16. See, e.g., In re Waste Mgmt. Sec. Litig., 194 F.Supp.2d 590, 596 (S.D. Tex. 2002) (“There is no express statement by Congress that it was modifying the traditional rule prohibiting removal of cases brought under the 1933 Act. Congress could easily have made a statement in SLUSA expressly modifying this provision had it so intended.”).
20. Rubin, 2007 U.S. Dist. LEXIS 17671, at *11-12. But see Nitoso, 2012 U.S. Dist. LEXIS 158049, at *21 (holding that 1933 Act claims are not removable but acknowledging that Section 77v(a) is inconsistent with Section 77p(b)).
22. 2007 U.S. Dist. LEXIS 119924. See also Roemer v. Vonage Holdings, No. 07-178(FWJ), 2007 U.S. Dist. LEXIS 8565, at *12 (D.N.J. Feb. 5, 2007) (stating without analysis that Section 77v(a) “grants exclusive jurisdiction to federal courts over all covered class actions regardless of whether they raise state law claims.”).
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