New York State Supreme Court Stays State Securities Class Action Despite Differences from Parallel First-Filed Federal Action

New York Supreme Court Justice Barry R. Ostrager's recent decision in *In re NIO Inc. Securities Litigation*, No. 0653422/2019 (N.Y. Sup. Ct. Aug. 21, 2020) ("*In re NIO*") represents a significantly favorable outcome for companies facing parallel claims in federal and state courts under the Securities Act of 1933 (the "Securities Act"). Justice Ostrager initially stayed the proceeding pending resolution of the parallel first-filed federal action. On August 21, 2020, Justice Ostrager declined to vacate his stay despite plaintiffs' argument that the proposed consolidated amended complaint in the state action included different alleged misstatements and different defendants than the parallel first-filed federal action.

I. Background

On March 20, 2018, the United States Supreme Court unanimously held in *Cyan, Inc.* v. *Beaver County Employees Retirement Fund,* 138 S. Ct. 1061 (2018), that (i) the Securities Litigation Uniform Standards Act did not disturb the concurrent jurisdiction of state and federal courts provided by the Securities Act and (ii) Securities Act claims are not removable from state to federal court. Following *Cyan*, there has been an increasing trend of duplicative Securities Act class actions being filed in both state and federal courts. This trend has increased the prospect of: (i) inconsistent rulings in the state and federal courts; (ii) waste of judicial resources adjudicating identical issues; and (iii) undue prejudice to defendants of being forced to litigate in multiple venues. Defendants facing such parallel actions frequently seek a stay of the second-filed state court action in favor of the first-filed federal action.

II. Justice Ostrager's Decision in *In re NIO*

NIO, Inc. ("NIO") is a Shanghai-based electric car company. NIO's initial public offering ("IPO") took place on September 12, 2018 and generated over $1 billion in net proceeds for the company. On March 5, 2019, six months after the IPO, NIO reported that it had a net loss overall for the year and that deliveries of its cars had slowed in January and February 2019. Following this news, on March 12, 2019, shareholders filed Securities Act class action lawsuits in federal courts in New York and California that were subsequently consolidated in the Eastern District of New York (collectively, the "Federal Action"), alleging that NIO's IPO materials were false or misleading for failing to disclose the likelihood of this downturn. On June 11, 2019, different shareholders filed similar Securities Act class action lawsuits in the New York State Supreme Court (collectively, the "State Action"). The State Action defendants moved for all proceedings to be stayed, arguing that the Federal Action was filed first and had the potential to resolve all of the shareholders' claims arising out of NIO's IPO. The State Action plaintiffs argued against the stay, observing that the State Action was more advanced than the Federal Action and there was not complete overlap of the defendants named in both actions. The State Action plaintiffs further accused the defendants of engaging in forum shopping. On December 13, 2019, Justice Ostrager granted the defendants' motion to stay that case in favor of the Federal Action. Justice Ostrager concluded that "[i]t would manifestly be a waste of judicial resources to have duplicative claims pending in two different courts."[1]

On May 18, 2020, the lead plaintiff in the Federal Action filed an amended complaint, alleging that NIO falsely represented that the company was building a manufacturing facility in China. On May 29, 2020, the State Action plaintiffs seized upon the amended allegations and moved to vacate the stay. The State Action plaintiffs supported their application by filing a proposed consolidated amended complaint that removed the manufacturing facility theory of liability, alleged misstatements about design problems and subsidy reduction, and included

[1] *In re NIO*, Order Granting Defs.' Mot. To Stay, at 1 (NYSCEF Doc. No. 86).

defendants not named in the Federal Action complaint. The State Action plaintiffs argued that, "because the [Federal Action] Complaint is incapable of resolving any of the Securities Act claims against all defendants in this action, the prior basis for temporarily staying this action no longer exists."[2]

Justice Ostrager declined to vacate the stay because the plaintiffs failed to show that the legal strategy being pursued in the Federal Action would prejudice the interests of the purported class.[3] The court rejected the State Action plaintiffs' argument that the Supreme Court's decision in *Cyan* overruled the controlling New York law governing the propriety of a stay. Prior New York appellate decisions had held (before *Cyan*) that a stay of a subsequently-filed action "is appropriate even though the second action asserts different legal theories when both cases arise out of the same transaction and seek to recover for the same alleged harm based on the same underlying events."[4]. Importantly, Justice Ostrager refused to lift his previously-ordered stay despite finding that the "plaintiffs have asserted the non-frivolous claim that the alleged nondisclosure of design problems and subsidy reductions in the registration statement are potentially actionable."[5]

III. Implications

Justice Ostrager's decision in *In re NIO* rejects a popular tactic of pleading some semblance of a difference between parallel Securities Act cases in federal and state court to defeat a stay of the second-filed matter. The State Action plaintiffs immediately filed a Notice of Entry and, on September 21, 2020, filed a Notice of Appeal from Justice Ostrager's decision. Should the decision stand on appeal—and/or be followed by other Justices faced with analogous situations—Justice Ostrager's rationale for maintaining the stay of proceedings could become an additional arrow in the quiver of defense attorneys and defendants facing duplicative Securities Act lawsuits in federal and state courts.

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If you have any questions about the issues addressed in this memorandum, or if you would like a copy of any of the materials mentioned in it, please do not hesitate to call or email Joel Kurtzberg at 212.701.3120 or jkurtzberg@cahill.com; Peter J. Linken at 212.701.3715 or plinken@cahill.com; or G. Kevin Judy II at 212.701.3499 or kjudy@cahill.com; or email publications@cahill.com.

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[2] *In re NIO*, Mem. Of Law In Supp. Of Pls.' Mot. To Vacate The Temporary Stay, at 4 (NYSCEF Doc. No. 92).

[3] *In re NIO*, Order Den. Pls.' Mot. To Vacate The Temporary Stay, at 1 (NYSCEF Doc. No. 102).

[4] *Id.* at 1–2 (internal quotation marks omitted) (citing *Syncora Guar. Inc.* v. *J.P. Morgan Sec. LLC,* 110 A.D.3d 87, 96-97 (1st Dep't 2013)).

[5] *Id.* at 2.

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