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Ninth Circuit grants rare mandamus relief regarding PSLRA plaintiff appointment

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On July 23, 2021, a Ninth Circuit panel vacated a district court order appointing a lead plaintiff in a consolidated securities fraud action. The panel found that the district court improperly required the presumptive lead plaintiff to prove its own adequacy under the PSLRA, rather than requiring the competing movants to prove that the presumptive lead plaintiff was inadequate.

In 2020, multiple plaintiffs filed federal securities lawsuits against Nikola Corporation and certain other defendants on the heels of issuance of a short-seller report. *In re Mersho*, No. 20-73819, slip op. at 5 (9th Cir. July 23, 2021). The district court consolidated these actions and then addressed the process under the Private Securities Litigation Reform Act (PSLRA) to appoint a lead plaintiff. *Id.* at 6. The district court first identified the presumptive lead plaintiff, i.e., the movant "with the largest financial interest and who has made a prima facie showing of adequacy and typicality." *Id.* Here, the presumptive lead plaintiff was Nikola Investment Group II (Group II), a group comprised of three investors that jointly applied for appointment with a claimed combined $6 million interest. *Id.* The district court held that Group II had made a prima facie showing of adequacy and typicality. *Id.* But the district court declined to appoint Group II, finding that the investment group members had not made clear how they "found each other" and appeared to have "joined solely for purposes of litigation," which gave the court "misgivings" about the group's cohesion. *Id.* at 7-8. After finding that other plaintiffs had not demonstrated adequacy and typicality, the court settled on the movant with the fourth-largest claimed loss. *Id.* at 8. The members of the investment group petitioned for a writ of mandamus to vacate the court's order, clarify that groups are permitted to serve as lead plaintiff under the PSLRA, and have Group II appointed as lead plaintiff instead. *Id.*

The Ninth Circuit granted the writ and vacated the district court's order. Before turning to the merits, the court highlighted that had each of the three members of the investment group moved for lead plaintiff ***individually***, they would have had the first, second, and fourth largest financial interests. *Id.* at 6. The panel then held the district court's decision reflected clear legal error—the threshold factor for mandamus relief. The panel explained that the statutory "three-step process for the selection of lead plaintiff" is "neither overly complex nor ambiguous." *Id.* at 11(internal citation and quotation marks omitted). The panel indicated that the PSLRA (1) allows a group to move for appointment, (2) requires the district court to determine "which movant has the largest alleged losses" and whether it "has made a prima facie showing of adequacy and typicality," and (3) allows for competing movants to then rebut the presumption of adequacy and typicality with "proof." *Id.* at 11-12.

The panel held the district court clearly erred because it "did not give effect to the presumption" and "effectively left the burden on Group II to prove adequacy at step three." *Id.* at 15. According to the panel, the district court penalized the presumptive lead plaintiff "for not explaining how [its members] found each other," indicating that the district court had "continued to place the burden on [it] to prove adequacy" at a point in the process where challengers bore the burden of proof. *Id.* Moreover, the panel held that a district court's "[m]isgivings are not evidence." *Id.* at 15-16. Rather, competing movants must point to "evidence of inadequacy" and "convince the district court" that the lead plaintiff is not adequate. *Id.* at 16.

Here, the panel found that the district court appeared to be persuaded by decisions from other courts that have expressed a preference for members of an investment group to "have a pre-litigation relationship." *Id.* The panel found that the district court "pointed to no evidence to support its decision" rejecting Group II's appointment, however. *Id.* The

panel also noted that the result—a lead plaintiff with losses "less than half or one-third of" the respective individuals in the investment group—was "troubling" and "incongruous" in light of the PSLRA's presumption that those "investors with the largest stake have the greatest incentive to supervise the litigation closely." *Id.* at 16 n.3.

Ultimately, the panel did not endorse or reject the group application. Rather, it found that district courts may still consider "pre-litigation relationships" and "cohesion" when addressing adequacy, so long as the district court "articulate[s] how the evidence proves inadequacy." *Id.* at 17.

Although the panel concluded that mandamus relief was warranted, it declined "to instruct the district court to appoint [the investor group] as lead plaintiff," leaving the determination of lead plaintiff to the district court on remand. *Id.* at 18, 20-21.

The panel included Circuit Judges Milan D. Smith, Jr. and Lawrence VanDyke, and District Judge Andrew P. Gordon.

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